

No. 12079

United States
Court of Appeals
for the Ninth Circuit

WILSHIRE & WESTERN SANDWICHES,
INC., a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Petition to Review a Decision of The Tax Court
of the United States

FILED

DEC 1 1948

PAUL P. O'BRIEN,

CLERK

No. 12079

United States
Court of Appeals
for the Ninth Circuit

WILSHIRE & WESTERN SANDWICHES,
INC., a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Petition to Review a Decision of The Tax Court
of the United States

INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

	PAGE
Answer	22
Answer to Amendment to Petition.....	26
Appearances	1
Certificate of Clerk to Transcript of Record...	321
Decision	41
Deposition of Robert A. Odell.....	234
—direct	235
—cross	246
—redirect	252
Designation of Record	319
Docket Entries	1
Findings of Fact and Opinion, Memorandum..	27
Motion to Amend Petition to Conform to Proof	24
Orders re Transmission of Exhibits in Original Form	317, 318
Petition for Redetermination of Deficiency...	4
Exhibit A—Notice of Deficiency.....	8

ii.

	PAGE
Petition for Review	42
Notice of Filing	47
Statement of Points Upon Which Petitioner Intends to Rely	322
Stipulation of Facts	256
Exhibit 1-A—Lease, April 26, 1941, between Robert Ashley Pettey and Julia Faye Pet- tey, Lessors, and Wm. H. Simon, Lessee..	264
Exhibit 2-B—Supplement to Lease dated May 2, 1941	286
Exhibit 3-C—Minutes of Meeting of Board of Directors on July 14, 1941.....	289
Exhibit 4-D—Application for Permit to Issue Shares of Stock dated July 14, 1941....	298
Exhibit 5-E—Permit to Issue Shares of Stock, July 17, 1941.....	305
Exhibit 6-F—Copy of Assignment of Lease, July 14, 1941	306
Exhibit 7-G—Lease, Aug. 22, 1941, between Edna R. Vogel, Lessor, and the Petitioner	310
Transcript of Proceedings and Testimony.....	48
Opening Statement on behalf of:	
Petitioner	49
Respondent	53

Witnesses for Petitioner:

Aye, Elias J.

—direct 182

—cross 202

Carpenter, Harry B.

—direct 98, 111

—cross 145, 164

—redirect 173

—recross 177

Simon, William H.

—direct 58

—cross 78

—redirect 93

—recross 97

Tompkins, Charles B.

—direct 212

—cross 219

Witnesses for Respondent:

Whittaker, Benjamin H.

—direct 99

—cross 104

—redirect 109

Wignall, Fred

—direct 226

—cross 228

APPEARANCES

For Petitioner:

HENRY M. WEBSTER, C.P.A.,
MARTIN H. WEBSTER, Esq.,
PAUL ZIFFREN, Esq.,
JACOB SHEARER, Esq.

For Respondents:

R. E. MAIDEN, Esq.,
E. C. CROUTER, Esq.

Docket No. 10638

WILSHIRE & WESTERN SANDWICHES,
INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

1946

Apr. 24—Petition received and filed. Taxpayer notified. Fee paid.

Apr. 25—Copy of petition served on General Counsel.

May 29—Answer filed by General Counsel.

May 29—Request for hearing in Los Angeles, California filed by General Counsel.

1946

June 3—Notice issued placing proceeding on Los Angeles, California calendar. Service of answer and request made.

1947

July 31—Motion to change date of hearing to next calendar after September filed by taxpayer. Granted.

July 31—Hearing set 9/22/47 in Los Angeles, California.

Sept. 30—Hearing set 12/1/47 in Los Angeles, California.

Nov. 5—Appearance of Paul Ziffren and Jacob Shearer as counsel filed.

Dec. 3

& 4—Hearing had before Judge Disney on merits. Stipulation of facts filed.

Dec. 12—Hearing had before Judge Disney on merits. Motion of petitioner to amend petition to conform to the proof—Motion granted. Respondent to file amended answer within 15 days. This appeal tried at Los Angeles, Calif., December 3rd and 4th. See previous minutes. Motion to amend petition filed at hearing. Copies served. Briefs due 2/2/48. Reply briefs 2/25/48.

Dec. 19—Transcript of hearing 12/3/47 filed.

Dec. 19—Transcript of hearing 12/4/47 filed.

Dec. 26—Answer to amendment to petition filed by General Counsel. 12/29/47 Served.

1948

- Jan. 19—Deposition of Robert A. Odell filed. (1)
Served by notary.
- Jan. 20—Brief filed by taxpayer. 2/4/48 Copy
served.
- Feb. 3—Motion for leave to file the attached
brief, brief lodged, filed by General Coun-
sel. 2/4/48 Granted.
- Feb. 24—Motion for extension to 3/5/48 to file re-
ply brief, filed by taxpayer. 2/25/48
Granted as to both parties.
- Mar. 4—Reply brief filed by taxpayer. Copy
served.
- June 29—Memorandum findings of fact and opinion
rendered, Judge Disney. Decision will be
entered for the respondent. Copy served.
- June 29—Decision entered. Judge Disney. Div. 4.
- July 8—Transcript of hearing 12/12/47 filed.
- Sept. 20—Petition for review by U. S. Court of
Appeals for the Ninth Circuit, with as-
signments of error filed by taxpayer.
- Sept. 27—Proof of service filed.
- Oct. 1—Praecipe for record filed by taxpayer.
- Oct. 6—Designation of contents of record with
proof of service attached thereto, filed by
taxpayer.
- Oct. 7—Order re transmission of Joint Exhibits
8-H, 9-I and 10-J inclusive in physical
form to be transmitted with the appeal
record entered.

1948

- Oct. 8—Motion that Exhibits 11 to 31 inclusive remain in custody of the Clerk of The Tax Court until 15 days prior to trial and upon advice of counsel be transmitted to U. S. Court of Appeals for the Ninth Circuit in physical form, filed by General Counsel.
- Oct. 12—Order that Exhibits 11 to 31 inclusive remain in custody of the Clerk of The Tax Court until 15 days prior to trial and upon advice of counsel be transmitted to U. S. Court of Appeals for the 9th Circuit in physical form, entered. [2*]

The Tax Court of the United States

Docket No. 10638

WILSHIRE AND WESTERN SANDWICHES,
INC.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of

* Page numbering appearing at foot of page of original certified Transcript of Record.

deficiency (Bureau Symbols LA:IT:90D:PAK) dated January 31, 1946, and as a basis of its proceeding alleges as follows:

1. The petitioner is a California corporation with principal office at 3180 West Sixth Street, Los Angeles 5, California. The returns for the periods here involved were filed with the collector for the sixth district of California.

2. The notice of deficiency (a copy of which is attached and marked Exhibit "A") was mailed to the petitioner on January 31, 1946.

3. The taxes in controversy are income taxes for the calendar year 1942 in the amount of \$599.87 and for the calendar year 1943 in the amount of \$782.72; declared value excess profit tax for the calendar year 1943 in the amount of \$168.31; and excess profits taxes for the calendar year 1943 in the amount of \$1,797.05. [3]

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) In determining the taxable net income of the petitioner for the calendar years 1942 and 1943, the Commissioner erroneously disallowed a deduction for interest accrued in the amount of \$1,500 for 1942 and \$1,443.36 for 1943.

(b) In determining the excess profits net income of the petitioner for the calendar year 1943, the Commissioner erroneously disallowed a deduction for interest accrued in the amount of \$1,443.36.

(c) In all of the aforesaid determinations, the

Commissioner has erroneously considered moneys advanced by stockholders of petitioner as capital contributions rather than as loans.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) The original capitalization of petitioner was planned to and actually did consist of the issuance of 3,000 shares of capital stock at the par value of \$10.00 each, or a total of \$30,000 as capital contribution. Uncertainty existed at the time of incorporation as to exactly how much money would be needed by petitioner to erect the building in its business and to purchase the equipment required therefor, although it was thought that the \$30,000 capital would probably be sufficient. Accordingly, the incorporators of petitioner agreed to lend to petitioner such amounts of money as might additionally be required for these purposes, the loans to be repayable in two years, to bear interest at the rate of 6% per annum, and to be represented by promissory notes. Pursuant to such agreement, and upon it being learnt that [4] more than the original capital contribution of \$30,000 would be required to erect the building and install the equipment, some but not all of the stockholders of petitioner lent sums of money to petitioner aggregating \$25,000. All such loans were evidenced by promissory notes, were payable in two years, and bore interest at 6% per annum. Interest was in fact accrued and paid on these notes, the books of petitioner recorded the interest as an expense, and the advances to it by its stockholders as loans. The Commissioner has erro-

neously considered these loans as in fact capital contributions.

Wherefore, the petitioner prays that this Court may hear the proceeding and determine the deficiency due from the petitioner.

/s/ HENRY M. WEBSTER,

/s/ MARTIN H. WEBSTER,
Counsel for Petitioner.

State of California,
County of Los Angeles—ss:

Harry B. Carpenter, being duly sworn, says that he is President of petitioner corporation, that he is duly authorized to verify the foregoing petition; that he has read the foregoing petition, or had the same read to him, and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be on information and belief, and that those he believes to be true.

/s/ HARRY B. CARPENTER.

Subscribed and sworn to before me this 22nd day of April, 1946.

/s/ ROSE BABICH,
Notary Public.

My Commission Expires April 1, 1949. [5]

S *Wilshire & Western Sandwiches, Inc.*

EXHIBIT "A"

Copy

Treasury Department
Internal Revenue Service
417 South Hill Street
Los Angeles 13, California

LA:IT:90D:PAK

January 31, 1946

Wilshire and Western Sandwiches, Inc.
3180 West Sixth Street
Los Angeles 5, California

Gentlemen:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1941, 1942 and 1943 discloses a deficiency of \$1,382.59 for the taxable years ended December 31, 1942 and 1943, and an overassessment of \$602.47 for the taxable year ended December 31, 1941, and that the determination of your declared value excess-profits tax liability for the taxable year ended December 31, 1943, discloses a deficiency of \$168.31, and that the determination of your excess-profits tax liability for the taxable years ended December 31, 1942 and 1943, discloses a deficiency of \$1,797.05 for the taxable year ended December 31, 1943 and an overassessment of \$706.81 for the taxable year ended December 31, 1942, as shown in the statement attached.

Exhibit A—(Continued)

After careful consideration of your applications for relief under section 722 of the Internal Revenue Code filed on September 15, 1943 for the taxable years ended December 31, 1941 and December 31, 1942 it has been determined that you have not established your right to the relief therein requested. In accordance with the provisions of sections 272 and 732 of the Internal Revenue Code, notice is hereby given of the deficiencies mentioned and of the disallowance of the claims for refund asserted in your application for relief under section 722.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington, D. C., for a redetermination of the deficiencies mentioned.

Very truly yours,

JOSEPH D. NUNAN, JR.,
Commissioner,

By GEORGE D. MARTIN,
Internal Revenue Agent in
Charge.

Enclosures: Statement, Form of waiver, Form 843.

Exhibit A—(Continued)

STATEMENT

LA:IT:90D:PAK

Wilshire and Western Sandwiches, Inc.

3180 West Sixth Street

Los Angeles 5, California

Tax Liability for the Taxable Years Ended
December 31, 1941 to 1943, Inclusive

Income Tax

Year	Liability	Assessed	Overassessment	Deficiency
1941	\$ 469.81	\$ 1,072.28	\$602.47	
1942	2,591.47	1,991.60	.....	\$ 599.87
1943	2,898.61	2,115.89	.....	782.72
	<hr/>	<hr/>	<hr/>	<hr/>
Totals	\$ 5,959.89	\$ 5,179.77	\$602.47	\$1,382.59

Declared Value Excess-Profits Tax

1943	\$ 758.00	\$ 589.69	\$ 168.31
------	-----------	-----------	-------	-----------

Excess Profits Tax

1942	None	\$ 706.81	\$706.81	
1943	\$22,158.79	20,361.74	.....	\$1,797.05
	<hr/>	<hr/>	<hr/>	<hr/>
Totals	\$22,158.79	\$21,068.55	\$706.81	\$1,797.05

In making this determination of your tax liability, careful consideration has been given to the applications for relief filed on September 15, 1943, for the taxable years ended December 31, 1941 and 1942, to the report of examination dated November 9, 1944, to your protests dated March 26, 1945, and October 31, 1945, and to the statements made at conferences held.

Exhibit A—(Continued)

Careful consideration has been given to your applications for relief (forms 991) under Section 722(c) of the Internal Revenue Code wherein you claim refunds or credits as follows: [7]

Taxable		Bureau		Refund or
Year	Form No.	Serial No.	Filed	Credit Claimed
1941	991	25330	9-15-43	None
1942	991	25331	9-15-43	\$706.81

It is held that you have not established that the tax computed under Subchapter E of Chapter 2 of the Internal Revenue Code without the benefit of Section 722 of the Code, results in an excessive and discriminatory tax within the provisions of Section 722(a), (b) and (c) of the Code and that you have not established what would be a fair and just amount representing normal earnings to be used as a constructive average base period net income for the purposes of an excess profits tax based upon a comparison of normal earnings and earnings during the respective excess profits tax periods.

It is further held that you have not established any factors affecting your business which may be reasonably considered as resulting in an inadequate standard of normal earnings during the base period not inconsistent with principles underlying the provisions of subsection (c) of Section 722 of the Internal Revenue Code.

In your returns for the years 1942 and 1943 you claimed deductions in the respective amounts of \$1,500.00 and \$1,443.26 as interest paid on the indebtedness due to certain stockholders on amounts

Exhibit A—(Continued)

paid to the corporation by them. It is determined that such amounts of alleged interest are not deductible within the purview of Section 23(b) of the Internal Revenue Code.

The issue in your claim for refund (form 843) for the taxable year ended December 31, 1941, filed on February 24, 1945, for the allowance as deductions of items of expense aggregating \$2,859.70 is conceded and appropriate adjustments therefor is made herein.

The overassessment of income tax for the taxable year ended December 31, 1941, shown herein will be made the subject of a certificate of overassessment which will reach you in due course through the office of the collector of internal revenue for your district, and will be applied by that official in accordance with section 322(a) of the Internal Revenue Code.

The overassessment of excess profits tax for the taxable year ended December 31, 1942, shown herein, will be made the subject of a certificate of overassessment which will reach you in due course through the office of the collector of internal revenue for your district, and will be applied by that official in accordance with section 322(a) of the Internal Revenue Code, provided that you fully protect yourself against the running of the statute of limitations with respect to the apparent overassessment referred to in this letter, by filing with the collector of internal revenue for your district, a claim for refund on form [8] 843, a copy of which is enclosed, the basis of which may be as set forth herein.

Exhibit A—(Continued)

Adjustments to Net Income

Taxable Year Ended December 31, 1941

Net income as disclosed by return.....	\$5,096.88	
Additional deductions:		
(a) Overstatement of income.....	\$518.25	
(b) Prepaid expenses allowed.....	669.39	
(c) Depreciation	816.08	
(d) Franchise tax	74.73	
(e) Capital stock tax	781.25	2,859.70
		<hr/>
Net income adjusted		\$2,237.18

Explanation of Adjustments

(a) Included in gross income reported in your return is the amount of \$518.25 representing moneys credited to income but actually due to Mr. H. B. Carpenter. It has been determined that this amount does not constitute your income and the amount so reported is eliminated.

(b) Amounts charged to prepaid expenses, not previously claimed by you, applicable to this taxable year have been allowed as follows:

Additional rent	\$660.88
Office expense	60.00
Miscellaneous taxes	29.24
	<hr/>
Total	\$750.12
Less: Overstatement of insurance.....	80.73
	<hr/>
Adjustment as above	\$669.39

(c) Depreciation in the amount of \$816.09, not previously claimed by you, is allowed as represent-

Exhibit A—(Continued)

ing a reasonable allowance for depreciation for the taxable year under section 23(1) of the Internal Revenue Code.

(d) An additional deduction is allowed for franchise tax in the amount of \$74.73.

(e) A deduction is allowed for capital stock tax, not previously claimed by you, in the amount of \$781.25. [9]

Computation of Income Tax

Taxable Year Ended December 31, 1941

Net income adjusted	\$2,237.18
Surtax net income	2,237.18
Normal-tax net income	2,237.18
Income tax:	
Normal tax—15% of \$2,237.18	335.58
Surtax—6% of \$2,237.18	134.23
	<hr/>
Correct income tax liability.....	\$ 469.81
Income tax assessed:	
Original, account No. 420657	1,072.28
	<hr/>
Overassessment of income tax.....	\$ 602.47

Adjustments to Net Income

Taxable Year Ended December 31, 1942

Net income as disclosed by return.....	\$ 8,532.02
Unallowable deductions:	
(a) Franchise tax	\$ 92.65
(b) Interest disallowed	1,500.00
	<hr/>
Total	\$10,124.67
Additional deduction:	
(c) Capital stock tax	156.25
	<hr/>
Net income adjusted	\$ 9,968.42

Exhibit A—(Continued)

Explanation of Adjustments

(a) The deduction claimed for franchise tax is \$92.65 in excess of the amount allowable under section 23(c) of the Internal Revenue Code.

(b) This adjustment has been previously explained.

(c) An additional deduction is allowed for capital stock tax in the amount of \$156.25. [10]

Adjustments to Excess Profits Net Income

Taxable Year Ended December 31, 1942

Excess profits net income as disclosed by return.....\$ 9,282.02

Unallowable deductions:

(a) Franchise tax\$ 92.65

(b) Interest disallowed 1,500.00 1,592.65

Total\$10,874.67

Additional deductions:

(c) Capital stock tax\$ 156.25

(d) 50% of interest on borrowed capital 750.00 906.25

Excess profits net income adjusted.....\$ 9,968.42

Explanation of Adjustments

(a) (b) and (c) These adjustments are the same as made to net income and previously explained.

(d) In computing the amount of excess profits net income shown in your return you decreased the deduction for interest by \$750.00 as representing 50 per centum of interest on borrowed capital as provided in section 711(a)(2)(B) of the Internal Revenue Code. It has been determined, under item (b) above, that the deduction claimed for interest on

Exhibit A—(Continued)

borrowed capital does not represent a proper deduction under section 23(b) of the Internal Revenue Code. Accordingly, the reduction of interest made by you is reversed.

Adjustments to Invested Capital

Taxable Year Ended December 31, 1942

Invested capital as disclosed by return.....	\$43,708.38	
Additions:		
(a) Money paid in for stock or as contribution to capital	\$25,000.00	
(b) 25% of new capital.....	13,750.00	
(c) Accumulated earnings and profits increased	558.99	39,308.99
Total		\$83,017.37
Reduction:		
(d) Average borrowed invested capital disallowed....	12,500.00	
Invested capital adjusted		\$70,517.37

Explanation of Adjustments

(a) and (d) It has been determined that the amount of \$25,000.00 shown in your return as borrowed capital, constitutes money paid in for stock or as a contribution to capital. Accordingly, the amount of \$25,000.00 is added to the equity invested capital shown in your return and the amount of average borrowed invested capital, \$12,500.00, claimed in your return is disallowed.

(b) There is added to your invested capital the amount of \$13,750.00 representing 25 per cent of new capital paid in during a taxable year beginning after December 31, 1940, in the amount of \$55,000.00, not previously claimed by you, in accordance with section 718(a)(6) of the Internal Revenue Code.

Exhibit A—(Continued)

(c) It has been determined that the amount of accumulated earnings and profits at the beginning of the taxable year was \$1,767.37 instead of the amount, \$1,208.38, shown by your return or an increase of \$558.99.

Computation of Excess Profits Tax

Taxable Year Ended December 31, 1942

Excess profits net income.....	\$ 9,968.42	
Less: Specific exemption	\$5,000.00	
Excess profits credit (8% of \$70,517.37 invested capital)	5,641.39	10,641.39
Adjusted excess profits net income.....	\$ 0.00	
Correct excess profits tax liability.....	0.00	
Excess profits tax assessed:		
Original, account No. 21079		706.81
Overassessment of excess profits tax.....	\$ 706.81	

Computation of Income Tax

Taxable Year Ended December 31, 1942

Net income adjusted	\$ 9,968.42	
Less: Income subject to excess profits tax.....	0.00	
Surtax net income	\$ 9,968.42	
Normal-tax net income	9,968.42	
Income tax:		
Normal tax:		
15% of \$5,000.00.....	\$750.00	
17% of \$4,968.42.....	844.63	1,594.63
Surtax:		
10% of \$9,968.42.....		996.84
Correct income tax liability	\$ 2,591.47	
Income tax assessed:		
Original, account No. 20696		1,991.60
Deficiency of income tax.....	\$ 599.87	

Exhibit A—(Continued)

Adjustments to Net Income

Taxable Year Ended December 31, 1943

Net income as disclosed by return.....	\$33,934.66
Unallowable deductions:	
(a) Accrued franchise tax disallowed....	\$1,206.82
(b) Interest disallowed	1,443.36
	<hr/>
Total	\$36,584.84
Additional deduction:	
(c) Capital stock tax	100.00
	<hr/>
Net income adjusted	\$36,484.84

Explanation of Adjustments

(a) In your return a deduction was claimed for accrued franchise tax in the amount of \$1,206.82. It has been determined that the liability for this tax did not accrue during the taxable year and the deduction claimed is, accordingly, disallowed. [13]

(b) This adjustment has been previously explained.

(c) An additional deduction is allowed for capital stock tax in the amount of \$100.00.

Computation of Declared Value Excess-Profits Tax

Taxable Year Ended December 31, 1943

Net income adjusted	\$36,484.84
Less: 10% of \$250,000.00 value of capital stock as declared in your capital stock tax return for the year ended June 30, 1943	25,000.00
	<hr/>
Net income subject to declared value excess-profits tax..	\$11,484.84
Declared value excess-profits tax: 6.6% of \$11,484.84....	758.00
Correct declared value excess-profits tax liability.....	758.00
Declared value excess-profits tax assessed:	
Original, account No. 411070	589.69
	<hr/>
Deficiency of declared value excess-profits tax.....	\$ 168.31

Exhibit A—(Continued)

Adjustments to Excess Profits Net Income
Taxable Year Ended December 31, 1943

Excess profits net income as disclosed by return.....	\$33,806.96	
Unallowable deductions:		
(a) Accrued franchise tax disallowed....	\$1,206.82	
(b) Interest disallowed	1,443.36	
(c) Decrease in deductions for declared value excess-profits tax	91.38	2,741.56
Total		\$36,548.52
Additional deductions:		
(d) Capital stock tax	\$100.00	
(e) 50% of interest on borrowed capital....	721.68	821.68
Excess profits net income adjusted.....		\$35,726.84

Explanation of Adjustments

(a) (b) and (d) These adjustments are the same as made to net income and previously explained.

(c) In computing the amount of excess profits net income shown in your return you claimed a deduction for declared value excess-profits tax in the amount of \$849.38. It has been determined that the correct deduction for declared value excess-profits tax for this taxable year was \$758.00, or a decrease of \$91.38.

(e) In computing the amount of excess profits net income shown in your return you decreased the deduction for interest by \$721.68 as representing 50 per centum of interest on borrowed capital as provided in section 711(a)(2)(B) of the Internal Revenue Code. It has been determined, under item (b) above, that the deduction claimed for interest does not represent a proper deduction under section 23(b) of the

Exhibit A—(Continued)

Internal Revenue Code. Accordingly, the reduction of interest, made in your return, is reversed.

Adjustments to Invested Capital

Taxable Year Ended December 31, 1943

Invested capital as disclosed by return.....	\$45,862.67	
Additions:		
(a) Money paid in for stock or as con- tribution to capital	\$25,000.00	
(b) 25% of new capital	13,750.00	
(c) Increase in accumulated earnings and profits	461.77	39,211.77
Total		\$85,074.44
Reduction:		
(d) Average borrowed invested capital disallowed....	8,750.00	
Invested capital adjusted		\$76,324.44

Explanation of Adjustments

(a) It has been determined that the amount of \$25,000.00 represents money paid in for stock instead constituting borrowed capital as claimed in your return. Accordingly, the amount of equity invested capital shown in your return is increased by \$25,000.00.

(b) There is added to the equity invested capital shown in your return the amount of \$13,750.00 representing 25 per cent of new capital, \$55,000.00, paid in during a taxable year beginning after December 31, 1940, not previously claimed by you, in accordance with section 718(a)(6) of the Internal Revenue Code.

Exhibit A—(Continued)

(c) It has been determined that the amount of accumulated earnings and profits at the beginning of the taxable year was \$7,574.44 instead of the amount, \$7,112.67, shown by your return, or an increase of \$461.77.

(d) In computing the amount of invested capital shown by your return you included the amount of \$8,750.00 as representing average borrowed invested capital resulting from money paid in by stockholders and claimed by you to represent borrowed capital. It has been determined, in item (a) above, that the money paid in by stockholders constitutes money paid in for stock or as a contribution to capital. Accordingly, the amount of average borrowed invested capital reported in your return on account of this transaction, \$8,750.00, is reversed.

Computation of Excess Profits Tax

Taxable Year Ended December 31, 1943

Excess profits net income	\$35,726.84	
Less: Specific exemption	\$5,000.00	
Excess profits credit (8% of \$76,324.44		
invested capital)	6,105.96	11,105.96
		<hr/>
Adjusted excess profits net income.....	\$24,620.88	
Excess profits tax: 90% of \$24,620.88.....	22,158.79	
(Limitation under section 710(a)(1)(B)		
not applicable)		
Correct excess profits tax liability.....	22,158.79	
Excess profits tax assessed:		
Original, account No. 400310.....	20,361.74	
		<hr/>
Deficiency of excess profits tax.....	\$ 1,797.05	

Exhibit A—(Continued)

Computation of Income Tax

Taxable Year Ended December 31, 1943

Net income adjusted		\$36,484.84
Less: Declared value excess-profits tax.....	\$ 758.00	
Income subject to excess profits tax.....	24,620.88	25,378.88
		<hr/>
Surtax net income		\$11,105.96
Normal-tax net income		\$11,105.96
Income tax:		
Normal tax:		
15% of \$5,000.00.....	\$ 750.00	
17% of \$6,105.96.....	1,038.01	\$ 1,788.01
		<hr/>
Surtax:		
10% of \$11,105.96.....		1,110.60
		<hr/>
Correct income tax liability.....	\$ 2,898.61	
Income tax assessed:		
Original, account No. 411070		2,115.89
		<hr/>
Deficiency of income tax.....	\$ 782.72	

[Endorsed]: T.C.U.S. Filed April 24, 1946. [17]

[Title of Tax Court and Cause.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

1, 2, and 3. Admits the allegations contained in paragraphs 1, 2, and 3 of the petition.

4. Denies the allegations of error contained in subparagraphs (a), (b), and (c) of paragraph 4 of the petition.

5. Denies the allegations contained in subparagraph (a) of paragraph 5 of the petition.

6. Denies each and every allegation contained in the petition not hereinbefore specifically admitted or denied.

Wherefore, it is prayed that the determination of the [18] Commissioner be approved.

/s/ J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Of counsel:

B. H. NEBLETT,
Division Counsel.

E. C. CROUTER,
R. E. MAIDEN, JR.,
Special Attorneys,
Bureau of Internal Revenue.

REM/emb 5/23/46

[Endorsed]: T.C.U.S. Filed May 29, 1946. [19]

[Title of Tax Court and Cause.]

MOTION TO AMEND PETITION TO
CONFORM TO PROOF

Comes now the Petitioner, by its attorney, Martin H. Webster, and moves this honorable Court to grant the said Petitioner leave to file an amendment to the petition already on file in this cause, under which amendment paragraph 5 (a) of the original petition shall be stricken therefrom and the following paragraph 5 (a) substituted therefor:

“5. The facts upon which the Petitioner relies as the basis of this proceeding are as follows:

(a) Uncertainty existed at the time of incorporation of Petitioner as to exactly how much money would be needed by Petitioner to erect a building for its business and to purchase the equipment required therefor, although it was thought that Thirty Thousand Dollars (\$30,000) would probably be sufficient. Accordingly, the [20] original capitalization of Petitioner was planned to consist of the issuance of One Thousand Five Hundred (1500) shares of capital stock at the par value of Ten Dollars (\$10.00) each, or a total of Fifteen Thousand Dollars (\$15,000) as a capital contribution, and approximately Fifteen Thousand Dollars (\$15,000) from the stockholders of Petitioner as loans. A total of Fifty-Five Thousand Dollars (\$55,000) was, in fact, required for the construction of the building and the equipment thereof. Thirty Thousand Dollars (\$30,000) of this

requirement was satisfied by the issuance by the corporation of Three Thousand (3000) shares of its common stock at the par value of Ten Dollars (\$10.00) per share; and the balance of the issuance by Petitioner of Twenty-Five Thousand Dollars (\$25,000) of its promissory notes, repayable in two years, bearing interest at the rate of six percent per annum. Interest was in fact accrued and paid on these notes, the books of Petitioner recorded the interest as an expense, and the advances to it by its stockholders as loans. The Commissioner has erroneously considered these loans as in fact capital contributions.” [21]

The reason for this motion is that the proof in the trial of this matter differs from the allegations contained in paragraph 5 (a) of the original petition, and this motion is made in order to conform said pleading to the proof.

Respectfully submitted,

/s/ MARTIN H. WEBSTER,
Counsel for Petitioner.

Dated: December 8, 1947.

[Endorsed]: T.C.U.S. Filed Dec. 12, 1947. [22]

[Title of Tax Court and Cause.]

ANSWER TO THE AMENDMENT TO
PETITION

The Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, for answer to the amendment to paragraph 5(a) of the original petition of the above-named taxpayer, says:

5(a). Denies the allegations contained in paragraph 5(a) of the amendment to the original petition.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ CHARLES OLIPHANT,
Chief Counsel,
Bureau of Internal Revenue.

Of counsel:

B. H. NEBLETT,
Division Counsel.

E. C. CROUTER,
R. E. MAIDEN, JR.,
Special Attorneys,
Bureau of Internal Revenue.

REM/vp 12/23/47

[Endorsed]: T.C.U.S. Filed Dec. 26, 1947. [23]

The Tax Court of the United States

Wilshire and Western Sandwiches, Inc., Petitioner,
v. Commissioner of Internal Revenue, Re-
spondent.

DOCKET No. 10638

Martin H. Webster, Esq., and Jacob Shearer,
Esq., for the petitioner.

R. E. Maiden, Jr., Esq., for the respondent.

MEMORANDUM FINDINGS OF FACT
AND OPINION

Disney, Judge: This proceeding involves deficiencies of \$599.87 and \$782.72 in income tax for the years 1942 and 1943, respectively, and a deficiency of \$168.31 in declared value excess profits tax and \$1,797.05 in excess profits tax for 1943. The issue is whether the respondent erred in disallowing as deductions for interest \$1,500 in 1942 and \$1,443.36 in 1943. The stipulation of facts filed by the parties is incorporated herein by reference as part of our findings of fact. [24]

FINDINGS OF FACT

The petitioner was incorporated on March 24, 1941, under the laws of California, with an authorized capital stock of 7,500 shares of common stock, par value \$10 each, for the purpose of engaging in the drive-in restaurant business. The incorporators of petitioner were M. A. McDonnell, William H. Simon, Mike Lyman, and Harry B. Carpenter. Its articles of incorporation empowered petitioner, among other things, to borrow

money and issue its notes therefor. It kept its books and prepared its returns on the accrual basis. It filed its returns for the taxable years with the collector for the sixth district of California.

Discussions resulting in the formation of petitioner started the early part of 1941. The original plan was to operate a combination drive-in and restaurant and cocktail room at Wilshire and Western Avenues, as a substitute for an old drive-in restaurant then being operated by Carpenter a block away. A lease was negotiated under the terms of which the lessor was to erect suitable improvements at a cost of about \$75,000. Carpenter did not desire to operate a combination restaurant on account of its size. In the meantime, Simon, acting for himself, negotiated a lease for another corner of Wilshire and Western Avenues for the purpose of operating a drive-in restaurant. Thereafter, but before petitioner was incorporated, the interested parties abandoned the plan under consideration and decided to construct a drive-in restaurant on the lot covered by the lease negotiated by Simon.

About April 1941 petitioner's incorporators discussed for the first time the question of financing the construction of the restaurant out of advances by them to petitioner for the purchase of its stock and as loans. The original [25] intention was to make advances totaling \$30,000 for stock and loans on an equal basis. The individuals desired to be in a position to participate with general creditors for part of their investment in the event petitioner's

business was not successful. In addition, they regarded a loan to be a better investment than stock to obtain returns on and repayment of their capital outlay. The individuals discussed the question of borrowing money from a bank and decided that they would rather receive the interest than to have petitioner pay it to a bank. They also discussed the tax benefit that would accrue to them and petitioner under the plan. Simon, who with his brother Mike Lyman was regarded as a unit in the transaction, considered his contemplated loan to be a safe investment. The same individuals, or some of them, entered into similar transactions for the same reasons with nine other corporations, one each in 1937 and 1939, six in 1941, and one in 1942. In all except two of the transactions, the notes received for loans were in proportion to the stock received.

Simon negotiated for, and on April 26, 1941, entered into, a lease for a corner lot at Wilshire Boulevard and Western Avenue, Los Angeles, for a period of 15 years. The lease provided for the improvement of the premises by a drive-in restaurant building at a cost of not less than \$30,000. The lease was acquired by Simon with the understanding that he would assign it to petitioner, and was assigned by him to petitioner in July 1941. The understanding was that Carpenter would supervise the construction of the building and operate the business. Three of the four individuals estimated that the improvements, including equipment, would cost about \$30,000. Carpenter, the other individual,

first believed that the cost would be about \$50,000, and in [26] July 1941, concluded that the cost would be \$38,000 or \$39,000. Simon and Carpenter estimated that the cost of the equipment would about equal the cost of the building.

About June 15, 1941, bids were solicited for the construction of the building on the leased premises, and on July 10, 1941, a contract was entered into for the construction of a building at a cost of \$22,651. The construction work was substantially completed about October 25, 1941, and the restaurant was opened for business about November 5, 1941.

The incorporators of petitioner made the following payments, totaling \$55,000, to petitioner in 1941 under the plan previously adopted by them.

	McDonnell	Simon	Lyman	Carpenter
May	\$3,333.33	\$	\$	\$
June	.....	1,666.67	1,666.66	3,333.34
August	.....	2,500.00	2,500.00	.....
September	5,000.00	.....	.....	5,000.00
October	.....	2,500.00	2,500.00	.....
Nov. 13	.....	2,500.00	2,500.00	.....
Nov. 19	10,000.00	.....	.....	5,000.00

The payments made on November 13th and 19th were agreed upon at an informal meeting held on November 12. At the same meeting the parties reached an agreement on the division of the advances between stock and notes. At the time the advances prior to November were made, the individuals intended that stock would be issued for one-half thereof, and notes for the remainder. No receipts were given by petitioner for the advances.

The money was first used to pay for the cost of

preparing plans and specifications for the building, and thereafter for the construction of the building and the equipment installed therein. The amount of \$38,114.68 was spent in 1941 for the building and \$17,515.78 for equipment, a total of \$55,630.46. In January 1942, the additional amount of \$2,375 was spent for building costs and, in that and the next month the additional amount of \$7,787.26 was spent for equipment. An expenditure of \$55,000 was necessary to place the restaurant in condition to open for business.

About February 1, 1942, petitioner borrowed \$10,000 from its stockholders to pay bills outstanding for the construction of the building and equipment of the restaurant. Carpenter and McDonnell each loaned one-third of the amount and Simon and Lyman each a one-sixth. Carpenter did not advise the other stockholders of the need for the money until a short time before the loans were made. The loans were paid on September 7, 1942, without interest.

About July 14, 1941, petitioner, pursuant to a resolution adopted by its Board of Directors on that day, filed an application with the Department of Investment of the State of California for permission to issue 1,500 shares of its stock for cash to its incorporators, and G. C. Jobson, and the remainder of its stock when authorized by its Board of Directors. The application recited that petitioner proposed to borrow from the stockholders or incorporators an additional amount sufficient to complete the building and equip it for the opera-

tion of a restaurant. At the same meeting, Carpenter was elected president and Simon vice president of petitioner. On July 17, 1941, the Commissioner of Corporations authorized petitioner to sell to the individuals named in its application for cash, at par, not to exceed 7,500 shares of its stock.

At a meeting of the Board of Directors of petitioner, the membership of which included the four incorporators, on November 13, 1941, a resolution was adopted, in accordance with an agreement reached at an informal meeting the [28] previous day, to issue to the incorporators for advances made by them promissory notes, totaling \$25,000, maturing in two years with interest at the rate of 6 per cent per annum, payable quarterly, and stock, totaling \$30,000, as follows:

	Carpenter	McDonnell	Simon	Lyman
Stock	\$10,000.00	\$10,000.00	\$5,000.00	\$5,000.00
Notes	8,333.34	8,333.33	4,166.67	4,166.66

The stock and notes authorized by the resolution were issued under date of November 13, 1941, and were delivered by December 5, 1941. In case of default in the payment of interest, the notes were to be immediately due and payable at the option of the holder. On November 25, 1941, 50 shares each of the stock issued to Simon and Lyman were transferred to Joseph Lardemar, in accordance with a gift made of the stock prior to November 13, 1941.

Carpenter expected the notes to be paid if petitioner had funds for that purpose. Simon expected the notes to be paid out of current earnings

and would not have insisted upon payment if payment would have caused financial hardship to petitioner.

Amounts, totaling \$3,055.86, were paid to the noteholders on December 1943, as interest on the notes to November 30, 1943. Like payments, aggregating \$682.10, were paid on March 23, 1945. The amounts were entered on the books of petitioner as a charge to an account under the name of "Interest Payable Accrued," which account was opened in February or March 1943, as of the close of 1942, with a credit to the account as interest accrued on the notes to December 31, 1942. The face amount of the notes was paid in full by payments of \$10,000 each, on April 21, 1943, and May 23, 1944, and \$5,000 [29] on March 23, 1945. The payment to the holder of each note was in proportion to his holdings of all of the notes.

In October 1941, Carpenter requested a certified public accountant to outline a set of books for petitioner's bookkeeper to install and use. After receiving the minutes of petitioner, the accountant prepared a list of entries. The journal entry showed that petitioner was incorporated with a capital of \$75,000, consisting of 7,500 shares of a par value of \$10 each. The outline of accounts to be used included an account for notes payable. Carpenter did not inform the accountant that part of the advances made by the incorporators was to be treated as loans to the corporation.

Petitioner's account under the name of "Capital Stock Unissued" contained a charge of \$75,000 and

a credit of \$55,000 on December 31, 1941. Its account "Stock Subscriptions Receivable" contained at that time a charge of \$55,000 and a credit for the same amount. The books also showed capital stock of \$75,000, of which \$55,000 was set aside against an account under the name of "Cash Special \$55,000." The books did not, on December 31, 1941, reflect any notes payable to stockholders. Sometime between January 15 and March 7, in 1942, the accountant took a trial balance from petitioner's books for the purpose of preparing petitioner's income tax returns for 1941. The balance sheet included in the income and declared value excess profits tax return listed as an asset capital stock subscriptions in the amount of \$55,000 and as a liability a like amount for capital stock. The return was signed by Carpenter, as president, and H. B. Carpenter, Jr., as treasurer, without objection to the return as prepared by the accountant or reading the return. Petitioner's president was aware that the affidavit he signed contained a statement that the return was correct. [30]

In April or May 1942, petitioner employed another accountant to examine its books. The accountant had knowledge that the stockholders of petitioner held notes of the corporation. He ascertained from a trial balance taken as of December 31, 1941, that the books did not reflect the notes issued to the stockholders under the date of November 13, 1941, and erroneously reflected the capital stock outstanding. After discussing the matter with Carpenter and Simon, the accountant made entries in

the books to reflect notes outstanding of \$25,000 and capital stock outstanding of \$30,000. While the accountant was preparing petitioner's income tax return for 1942, he ascertained that no amount had been accrued for interest on the notes. An appropriate account was then opened and the amount of \$1,687.50 was entered therein as interest accrued on the notes to the close of 1942. Thereafter interest was accrued on the notes monthly.

The earned surplus account of petitioner discloses credit balances of \$2,468.16, \$9,740.40, \$17,980.01, \$45,752.61, \$51,349.06, and 59,289.40 at the close of the years 1941 to 1946, inclusive. The account contains no charge for dividends.

Petitioner's president, who testified at the hearing, was at an undisclosed time indicted in a Federal district court in California for filing false and fraudulent individual returns and like returns for a firm doing business under the name of Carpenter's Drive-In. At the trial, Carpenter entered a plea of nolo contendere and paid a fine, imposed by the court. No sentence of imprisonment was imposed by the court.

In its returns for 1942 and 1943 the petitioner claimed \$1,500 and \$1,443.26, respectively, as deductions for interest on the notes held by its [31] stockholders. In his determination of the deficiencies the respondent held that the amounts were not deductible under section 23(b) of the Internal Revenue Code.

OPINION

The disagreement between the parties is whether the notes issued to the stockholders of petitioner constitute indebtedness within the meaning of section 23(b) of the Internal Revenue Code, as contended by petitioner, or investments in and contributions to capital of petitioner, as contended by the respondent. Petitioner contends that Cleveland Adolph Mayer Realty Corporation, 6 T.C. 730, is determinative of the issue here. The respondent cites *Edward G. Janeway*, 2 T.C. 197, *aff'd*, 147 Fed(2d) 602, as having facts similar to those prevailing here.

Promissory notes were issued for the amounts; the instruments and accrued interest thereon were belatedly entered in the corporate books as such; interest on and principal of the notes were eventually paid; and there is testimony in the record that the parties intended the amounts as loans. The question is factual and such evidence must be weighed with other facts of record to determine the true character of the amounts. *Joseph B. Thomas*, 2 T.C. 193; *Edward G. Janeway*, *supra*; *Doyle v. Mitchell Bros. Co.*, 247 U.S. 179.

The general plan was decided upon prior to any business activity of petitioner and was intended to meet capital outlays which are usually paid out of invested capital and/or secured indebtedness. Similar arrangements were made by the stockholders, or some of them, in connection with other corporations formed to engage in the restaurant business. No evidence was offered to [32] establish that the

individuals were lenders of money other than under plans such as the one here under consideration.

The advances here have few of the usual characteristics of commercial loans entered into in arm's length transactions. All of the amounts were paid in to provide petitioner with funds to start business, hence all of it was working capital. The original plan was to take stock and notes on an equal basis and three of the four interested parties estimated that an expenditure of about \$30,000 would be sufficient to open the restaurant for business. The amount of \$55,000 was required to place the restaurant in condition to commence business, yet there was no agreement to advance the final \$30,000 paid in until November 12, 1941, which was a week after the restaurant was opened for business, and until then no final agreement was reached on the proportions of the advances to be regarded as loans and for the purchase of stock, or the terms of the loans. The plan finally adopted and made effective on the division of the advances between stock and notes was not in accordance with the agreement originally entered into, which discloses that the parties were at all times in a position to divide the advances between stock and notes in any proportion. The portion regarded as a loan by each stockholder was in direct proportion to his holding of stock.

Carpenter committed petitioner to pay additional construction costs, in the amount of about \$10,000, without the consent of the other incorporators. Such amount was borrowed, without interest, from

the stockholders in direct proportion to stockholdings. The loans altered the ratio of stock to loans from 30-25 to 30-35, and is evidence that the individuals were not dealing with petitioner as "mere lenders." Some of the funds were advanced as early as [33] May 1941, yet no interest thereon was incurred by petitioner prior to November 13, 1941. In the meantime, there was no agreement on when interest would start, the rate of interest, or an agreement with petitioner on when the loans would mature, contrary to the manner loans are generally made.

The treatment of the notes on the books and payment of the obligations is significant. The notes were not entered in the books until April or May 1942, and although interest was payable quarterly, none was accrued on the books until 1943 and no interest was paid until December 1, 1943, or more than two years after the notes were executed. The terms of the instruments gave to the holders thereof the right to declare the principal and interest immediately due and payable upon default in the payment of interest when due. No evidence was offered that any of the note holders exercised the right. The final payment on the notes was not made until March 23, 1945, or more than sixteen months after maturity, and the payment made each time to each was in direct proportion to his holdings of all of the notes. No evidence was offered to show any demand for payment at maturity. The \$10,000 borrowed about February 1, 1942, without interest, was paid in full by one payment made on Septem-

ber 7, 1942, which was about fifteen months before the first interest payment was made on the notes. No additional capital was invested in the business, with the result that the notes were paid, as the parties intended, out of operating income.

The intent of the parties with respect to a part of the advances as bona fide loans, is reflected in testimony of Simon, who, with his brother, regarded as a unit in the transaction, and Carpenter. The former testified that he expected the note to be paid at maturity, but would not have insisted [34] upon payment if payment would result in financial hardship to petitioner. The latter did not expect payment unless petitioner had funds. It is apparent from the testimony that they did not intend to assert rights of a bona fide lender; instead regarded the amounts as being subject to the risks of the business and looked to repayment out of corporate earnings. There was no need to acquire an additional proprietary interest for the amounts, in view of the fact that the stock issued for remainder of the advances gave each stockholder the same control he would have had had the stock alone been issued.

The petitioner had earned surplus of about \$51,000 by the close of 1945, or double the amount of its outstanding stock, yet paid no dividends on its stock during that period, which strongly indicates that the stockholders looked to the notes for income on their investments and a partial return of capital.

Testimony is present that hazards of the restaurant business was one of the reasons for the

plan adopted and carried out. Other testimony requires us to refuse to accept it at its face value. Advances totaling \$65,000 were eventually made in a venture which three of the interested parties thought could be started in business by a capital outlay of only about \$30,000, and the third, Carpenter, about \$38,000. Simon thought the loan was safe and all of them preferred the plan over a bank loan for the amount covered by the notes. Such opinions and action is opposed to the idea that the parties had any great concern about the financial success of the business.

Further discussion of the facts seems unnecessary. The substance of the plan, which must prevail over the form thereof, was to make capital contributions, subject to an understanding of the participants, that they would be repaid in full if the petitioner had sufficient earnings to make the payments without financial hardship to it. Accordingly,

Decision will be entered for the respondent.

Entered June 29, 1948. [36]

(Seal)

The Tax Court of the United States

Docket No. 10638

WILSHIRE AND WESTERN SANDWICHES,
INC.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its Memorandum Findings of Fact and Opinion, entered June 29, 1948, it is

Ordered and Decided: That there are deficiencies in income tax of \$599.87 and \$782.72 for the years 1942 and 1943, respectively, and a deficiency of \$168.31 in declared value excess-profits tax and \$1,797.05 in excess profits tax for the year 1943.

(Seal) /s/ R. L. DISNEY,
Judge.

Entered June 29, 1948. [37]

In the United States Court of Appeals
for the Ninth Circuit

Tax Court Docket No. 10638

WILSHIRE & WESTERN SANDWICHES,
INC., a corporation,

Petitioner on Review,
vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

PETITION FOR REVIEW OF DECISION OF
THE TAX COURT OF THE UNITED STATES

To the Honorable Judges of the United States
Circuit Court of Appeals for the Ninth Circuit:

Comes now Wilshire & Western Sandwiches, Inc., a corporation, by Swarts, Tannenbaum, Ziffren & Steinberg and Jacob Shearer, its attorneys, and respectfully shows:

I.

The Petitioner herein referred to as the "taxpayer," is a resident of Los Angeles County in the State of California, and its address is 3180 West Sixth Street, Los Angeles 5, California.

The Respondent is the duly appointed, qualified, and acting Commissioner of Internal Revenue of the United [38] States; George J. Schoeneman, herein referred to as the "Commissioner."

The taxpayer filed income tax returns, excess profits tax returns and declared value excess profits tax returns for the taxable years 1942 and 1943

with the Collector of Internal Revenue for the Sixth District of California, whose office is located within the Ninth Judicial Circuit, wherein the taxpayer also resides.

II.

The Commissioner determined deficiencies of five hundred ninety eight dollars and eighty seven cents (\$598.87) and seven hundred eighty two dollars and seventy two cents (\$782.72) in the taxpayer's income tax for the years 1942 and 1943 respectively and determined deficiencies of one thousand seven hundred ninety seven dollars and five cents (\$1,797.05) and one hundred sixty eight dollars and thirty one cents (\$168.31) in the taxpayer's excess profits taxes and declared value excess profits taxes respectively for the year 1943 and on January 31, 1946, in accordance with the provisions of the applicable statute, sent to the taxpayer, by registered mail, a notice of the aforementioned deficiency.

Within ninety (90) days thereafter, the taxpayer filed a petition for review by the Tax Court. The case was tried and submitted and on June 29, 1948, the Tax Court promulgated a decision wherein it ordered and decided that [39] there were deficiencies in the amount of five hundred ninety eight dollars and eighty seven cents (\$598.87) and seven hundred eighty two dollars and seventy two cents (\$782.72) in the taxpayer's income taxes for the years 1942 and 1943, respectively, and deficiencies in the amounts of one thousand seven hundred ninety seven dollars and five cents (\$1,797.05)

and one hundred sixty eight dollars and thirty one cents (\$168.31) in the taxpayer's excess profits taxes and declared value excess profits taxes respectively for the taxable year 1943.

III.

The aforesaid deficiencies resulted from a determination by the Commissioner that the sum of fifteen hundred dollars (\$1,500.00) accrued in the year 1942 and of one thousand four hundred forty three dollars and twenty six cents (\$1,443.26) accrued in the year 1943, and paid by the taxpayer as interest on loans to it by its shareholders, was not deductible from gross income as interest on an indebtedness in determining its net income subject to tax. The capitalization of the taxpayer consisted of the issuance of three thousand (3,000) shares of capital stock at the par value of ten dollars (\$10.00) each, or a total of thirty thousand dollars (\$30,000.00) as capital contribution. In addition the incorporators of the taxpayer agreed to lend the taxpayer such amounts of money as might in the future be [40] found to be necessary for these purposes. Pursuant to this agreement, some of the stockholders of the taxpayer loaned sums of money to the taxpayer in the aggregate amount of twenty five thousand dollars (\$25,000.00). All such loans were evidenced by promissory notes, were payable in two (2) years and bore interest at the rate of six per cent (6%) per annum. Interest was in fact accrued and paid on these notes and the books of the corporation recorded the interest as an expense and the advances to it by its

stockholders as loans. The Commissioner contended that the amounts so loaned to the taxpayer were capital contributions and that consequently the amounts paid as interest were not paid as interest on an indebtedness and so not deductible by the taxpayer from its gross income in computing its net income subject to tax. The Commissioner's contention was upheld by the Tax Court and taxpayer says that in this the Tax Court committed error.

IV.

The taxpayer says in the record and proceedings before the Tax Court and in the decision and final order of redetermination rendered and entered by the Tax Court, manifest error occurred and intervened to the prejudice of the Petitioner and assigns and avers that the following errors and each of them occurred in said record, proceedings, decision and final order of redetermination and that upon [41] these it relies to reverse said decision and final order of determination so rendered and entered by the Tax Court, to wit:

1. The Tax Court erred in holding that the sum of fifteen hundred dollars (\$1,500.00) accrued in the year 1942 and of one thousand four hundred forty three dollars and twenty six cents (\$1,443.26) accrued in the year 1943 and paid by the taxpayer as interest on loans by its shareholders, was not deductible as interest on an indebtedness.

2. The Tax Court erred in refusing to hold that said sums mentioned above were interest on an indebtedness and as such were deductible from the

taxpayer's gross income in determining its net income subject to taxation.

3. The Tax Court erred in determining that there was a deficiency in the taxpayer's income taxes for the taxable years 1942 and 1943.

4. The Tax Court erred in determining that there was a deficiency in the taxpayer's excess profits tax for the taxable year 1943.

5. The Tax Court erred in determining that there was a deficiency in the taxpayer's declared value excess profits taxes for the year 1943.

Wherefore, the taxpayer petitions that the decision of the Tax Court of the United States be reviewed by the [42] United States Circuit Court of Appeals for the Ninth Circuit, that a transcript be prepared in accordance with the law and with the rules of said Court and transmitted to the Clerk of said Court for filing, and that appropriate action be taken by said Court to the end that the errors complained of may be reviewed and corrected.

SWARTS, TANNENBAUM, ZIFFREN
& STEINBERG and
JACOB SHEARER.

By /s/ JACOB SHEARER,
Attorney for Taxpayer.

[Endorsed]: T.C.U.S. Filed Sept. 20, 1948. [43]

[Title of U. S. Court of Appeals and Cause.]

NOTICE OF FILING PETITION FOR
REVIEW

To: Charles Oliphant, Chief Counsel of the Bureau
of Internal Revenue, Washington, D. C.

You will please take notice that on the 20th day
of September 1948, the Petitioner above named
filed with the Clerk of the Tax Court of the United
States at Washington, D. C., a petition for review
by the United States Circuit Court of Appeals for
the Ninth Circuit of the decision of the Tax Court
of the United States heretofore rendered in the
above entitled cause.

A copy of the petition for review as filed is here-
by attached and served upon you. [44]

Dated: this 20th day of September 1948.

SWARTS, TANNENBAUM, ZIFFREN
& STEINBERG and
JACOB SHEARER.

By /s/JACOB SHEARER,
Attorneys for Petitioner.

ACKNOWLEDGMENT OF SERVICE

Personal service of the foregoing notice together
with a copy of the petition for review is hereby
attached this 27th day of September 1948.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue, Coun-
sel for Respondent.

[Endorsed]: T.C.U.S. Filed Sept. 27, 1948. [45]

In The Tax Court of the United States

Docket No. 10638

WILSHIRE AND WESTERN SANDWICHES,
INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Court Room No. 229,
United States Post Office and
Court House Building,
Los Angeles, California.
December 3, 1947—2:30 p.m.

(Met pursuant to notice.)

Before: Honorable Richard L. Disney, Judge.

Appearances: Martin H. Webster—215 West Seventh Street, Los Angeles, California, and Jacob Shearer—650 South Spring Street, Los Angeles, California, appearing for the Petitioner. R. E. Maiden, Jr. (Honorable Charles Oliphant, Chief Counsel, Bureau of Internal Revenue)—appearing for the Respondent. [47]

PROCEEDINGS

The Clerk: Docket 10638, Wilshire and Western Sandwiches. Inc. For the Petitioner Mr. Paul Ziffren and Mr. Jacob Shearer.

Mr. Shearer: Mr. Jacob Shearer and Mr. Martin H. Webster. I think he is of record, too, counsel.

The Clerk: Yes.

Mr. Shearer: He was one of the original counsel.

The Court: Is he present?

Mr. Webster: I am.

The Clerk: Mr. R. E. Maiden, Jr. for the Respondent.

Mr. Webster: If your Honor please—

The Court: Just a moment. It seems to be a question as to whether certain deductions for interest were allowable because of the contention as to whether there were loans or capital contributions. That seems to be your situation. State the matter for the Petitioner.

OPENING STATEMENT ON BEHALF OF THE PETITIONER

By Mr. Webster:

Mr. Webster: Your Honor, the tax years involved are the calendar years 1941, 1942 and 1943. As your Honor has already stated, the issues arise—one, as to the question of deductibility of interest, and two, as to the computation of the excess profits tax credit.

The Court: Why do you mention 1941? It isn't [49] mentioned in the petition. The petition says 1942 and 1943.

Mr. Maiden: There is an over-assessment for 1941 not involved in this proceeding, if the Court please.

The Court: The Petitioner says nothing, so far as I can see, about over-assessments. I have no jurisdiction over assessments, anyway.

Mr. Webster: That is right, your Honor.

The Court: Proceed.

Mr. Webster: The question as to the excess profit tax computation arises by reason of the difference in computation. If the moneys in question are considered equity investment capital, which they would be were they found by this Court to represent investments for the purchase of stock or borrowed capital, which they would be, if the Court finds for the Petitioner that these moneys in question were loans.

Stating the issue very simply, it seems to the Petitioner that this case turns on a question of intent, as to the intent of four individuals at the time in 1941 when they formed a corporation for the purpose of operating a drive-in restaurant operation on Wilshire Boulevard and Western Avenue.

For this purpose they formed a corporation. They made an estimate as to the amount of money which would be required to construct the drive-in and equipment, and at that time, at the time that they made this first estimate and before [50] construction began they agreed among themselves that probably 50 per cent of the moneys so required would be contributed to the corporation and be considered by the corporation as for the purchase of stock.

That approximately 50 per cent, that is, the balance, was intended by these individuals to constitute a loan.

The actual construction of the drive-in com-

menced in July of 1941; shortly prior thereto a meeting had been held of the board of directors of this corporation. This was on July 14th of 1941. At that time the intent and agreement which I have just summarized was incorporated in those minutes, the minutes of that meeting.

Additionally, still just prior to the actual construction, the board of directors authorized an application to be filed with the Corporation Commissioner for permission to issue stock, and in this application again stated its general plan of having a part loan-part stock setup. A permit was granted on that basis.

Shortly after construction commenced, construction of the drive-in, it was found that the actual costs would be in excess of the estimates. Accordingly, rather than issue stock immediately upon the granting of the permit by the California Corporation Commissioner, the board of directors decided to withhold such issuance of stock until such time as they had a better idea of how much the total cost would be. [51] This actual figure was arrived at or believed to have been arrived at in November, in the middle of November of 1941.

It was at that time that the board of directors again convened and agreed upon the final issuance of stock to the extent of \$30,000.00. They also agreed that the balance of the amount which they had thus far contributed toward the cost of the drive-in would constitute a loan.

Within two or three weeks after the meeting notes were issued in the amount of the loan, total-

ing \$25,000.00, and stock certificates were duly issued in the amount of \$30,000.00.

Thereafter, all activities of the corporation and of the individuals were consistent with this part loan-part stock setup, except for the manner in which the books and tax returns were handled. And with respect to that, your Honor, we propose to place upon the stand the accountant who came in within six months after the books were first set up. He will testify to the errors which he saw and also testify further to the correcting of those errors which he completed within approximately six months after the errors had first been made and before any revenue agent came in to raise any issue here.

We propose further, your Honor, to present testimony bringing out, not only the presence of an intent on the part of these individuals to lend, but also a good business purpose, [52] making reasonable such an intent.

Your Honor, it was hoped at this time that a Mr. Odell, who was an attorney, the attorney who handled all of the corporate transactions, from its inception, and is still handling that corporation today—it was hoped he would be here to be able to testify as to certain dates, which but recently placed in issue, dates of actual delivery of stock certificates and actual delivery of notes. Mr. Odell, unfortunately, is ill. If your Honor please, I should like to make a motion at this time, even though it is a little out of sequence in an opening statement, that in the event it is considered necessary at the

conclusion of this case, conclusion of the presentation of this case, I should like to move that this Court grant permission to bring Mr. Odell in at a later date, probably next week. I anticipate he will be well enough to come in to testify to certain facts, in the event that it is considered that those facts have not been adequately brought out through the testimony that we propose to present now.

The Court: I won't pass upon that motion at this time. We will discuss that at the end of the trial.

Mr. Webster: Very good, your Honor. Certain of the facts, your Honor, have been stipulated to.

The Court: Let's hear the Respondent's statement. Have you finished the statement of issues? Let's hear the [53] Respondent's statement, and then go into the question of your stipulation.

OPENING STATEMENT ON BEHALF OF THE RESPONDENT

By Mr. Maiden:

Mr. Maiden: If it please the Court, of course, I am not apprised beyond the stipulated facts of what counsel expects to prove in this case, in support of their contention that certain of the advances made by these stockholders were, in fact, and in bona fides, loans to the corporation.

The stipulation of fact, which we have prepared, sets forth the formation of the corporation and one of the minutes and the permit filed with the Corporation Commissioner for the right to issue immediately 1500 shares of the stock, and the sub-

sequent right to issue an additional 5000 shares for cash; these shares having the value of \$10.00.

The articles of incorporation authorized the issuance of 7500 shares of a par value of \$10.00 per share.

It is the Respondent's position in this case that the advances—that no part of the advances made by these stockholders to the corporation were, in fact and in bona fides loans but that the entire amount of the advances made by these stockholders were investments in the business. And upon that determination the Respondent has disallowed deductions taken by the corporation in 1942 and 1943 for alleged interest payable on the purported loan obligations. [54]

I believe that is a sufficient statement from the Respondent as to our position in the case. We feel that the facts will support our contention that there were, in fact, no bona fide loans.

The Court: Put on your evidence for the Petitioner.

Mr. Webster: Your Honor, as has been mentioned, a stipulation has been entered into between Respondent and Petitioner incorporating, physically incorporating Exhibits 1-A through 7-G. In addition, counsel for Respondent is in possession of the original tax returns for the calendar years 1941, 1942 and 1943, which are not physically attached to the stipulation but which can be submitted at the same time. They are referred to in the stipulation and numbered respectively 8-H to 10-J.

Mr. Maiden: If the Court please, before the filing of this stipulation I note what appears to be a typographical error, which I would like to call to counsel's attention so we may correct it in ink before we hand in the stipulation.

Mr. Webster: Mr. Maiden, I have just checked that point and it seems proper.

Mr. Maiden: Your Honor, there seems to be an irreconcilable error in the stipulation. The part of it that is obviously in error, from my standpoint, is a copy of a permit filed with the Corporation Commissioner—

The Court: Why don't you strike that from your [55] stipulation and then later when you find out what is the fact file a separate short stipulation setting forth what the facts are?

Mr. Maiden: I could be wrong about it being an error, but I don't see how I can. I am willing to let the stipulation go in with the understanding that if this is an error I might call it to the Court's attention in my brief. I have not examined the original of this document. I have relied upon counsel's statement that it is a correct copy of the original.

The Court: Well, what if then you still don't agree on the matter?

Mr. Webster: I have examined the original document and believe this is an accurate copy. I am willing to stipulate to that effect, that we admit this stipulation, file the stipulation and in the event that the point now being raised by Mr. Maiden is accurate and that an error has been made, I will

stipulate that the change can be interlined in pencil in the exhibit.

Mr. Maiden: Your Honor, if the parties—if there is an error made and the parties are able to agree upon it, why, then we will call it to the Court's attention in the brief. Otherwise, the Respondent will pass it up. I don't think it is of any very obvious importance.

The Court: Then in your briefs state whether you [56] are in agreement on it.

Mr. Maiden: Yes, sir.

The Court: Make a point of that.

Mr. Maiden: Yes, sir.

The Court: If I hear nothing further about it, I will know you have concluded that you are in error and that the stipulation is correct.

Mr. Maiden: Yes. And in order to point up the particular place, I might state that the point in question occurs at page 7 of Exhibit 4-D to the stipulation, which will now be offered. It relates to whether or not the figure 5,000 at the top of that page should be 6,000 or the 5,000.

Now, at this time I offer the original and one copy of the stipulation of facts which the parties have entered into in this case.

The Court: Let the stipulation be filed and the facts therein set forth will be received in evidence. Now produce your three other exhibits referred to in your stipulation.

Mr. Maiden: Now, if the Court please, at this time in order to complete the stipulation I now offer in evidence as Exhibits Nos. 8-H, 9-I and

10-J, the Corporation Income and Declared Value Excess-Profits Returns filed by the Petitioner for the calendar years 1941, 1942 and 1943, and I ask that the Clerk so mark these exhibits as being a part [57] of the stipulation.

The Court: And the Petitioner joins in this offer of these three instruments?

Mr. Webster: Yes.

The Court: Be sure that the Clerk marks them separately.

Mr. Webster: The 1941 return will be Exhibit No. 8-H.

The Clerk: It has been so marked.

Mr. Maiden: The 1942 return will be marked 9-I?

The Clerk: That has been done.

Mr. Maiden: And the 1943 return will be marked 10-J?

The Clerk: Thank you.

(The documents above-referred to were received in evidence and marked Joint Exhibits 8-H, 9-I and 10-J.)

Mr. Maiden: If the Court please, inasmuch as these are original returns, I would like to have permission—

The Court: Permission is given to substitute photostatic copies.

Mr. Maiden: Thank you.

Mr. Webster: Mr. Simon. [58]

Whereupon,

WILLIAM H. SIMON,

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Clerk: Please tell us your name.

The Witness: William H. Simon.

Direct Examination

By Mr. Webster:

Q. Mr. Simon, you are in the restaurant business? A. Yes.

Q. And how long have you been in that business? A. Oh, somewhere over 30 years.

Q. Mike Lyman is your brother, is that correct? A. Yes.

Q. And he is in the restaurant business, also? A. He is.

Q. How long has he been in that business? A. Oh, since about 1919.

Q. Have you been in business together? A. Yes.

Q. In what proportion have you shared your business deals? A. 50-50.

Q. What kind of restaurants have you operated? [59]

A. Well, we operate drive-ins, grills, dairy lunch rooms, cafeterias, coffee shops.

Q. When did you first enter the drive-in restaurant business? A. Along about 1935.

Q. Are you familiar with doing business as a corporation? A. Yes.

(Testimony of William H. Simon.)

Q. When did you first commence doing business in corporate form?

A. Ever since we went in business.

Q. Well, now, have all drive-ins in which you have acquired interests been in the corporate form?

A. Yes.

Q. So that at least since 1935—

A. That is right.

Q. —your drive-in restaurants have been in corporation form? A. Yes.

Q. Have your other business ventures involving restaurants been as corporations? A. Yes.

Q. Can you state why you have done business in the corporate form?

A. We try to make each restaurant stand on its own feet. [60] In other words, if it is a separate corporation and if anything should happen to any particular restaurant it doesn't carry down the others, the rest.

Q. That is, you have also adopted a policy, apparently, of having a separate corporation for each restaurant location. A. That is right.

Q. You, Mr. Simon, have formed an opinion, I imagine, as to the safety or riskiness of the restaurant business. Will you kindly state what your opinion of the restaurant business is, in general, from that point of view?

A. It is a very hazardous business, the restaurant business.

Q. Have you ever operated a restaurant which failed?

(Testimony of William H. Simon.)

A. We never operated a restaurant that failed; we close a lot of restaurants.

Q. For what reason?

A. Lack of business, out moded.

Q. Mr. Simon, are you familiar with whether there is a difference between lending to a corporation and buying stock in that corporation?

A. I am.

Q. Would you kindly state what, in your opinion, that difference consists of?

A. Well, when you buy stock in a restaurant, in a corporation, you are subject to just your dividends. That is [61] Number 1. And you just come in as a common creditor; you just come in as a common creditor when you make a loan to a corporation. You don't freeze your money, you become—you are sure of getting your money back. If you don't make profit in that particular restaurant you can get it back out of depreciation.

Q. Let me clarify in my own mind what you stated with respect to your position as a stockholder. As a stockholder what is your understanding of your position in the event that the restaurant which the corporation, of which you are a stockholder,—what your position would be if that restaurant failed.

Mr. Maiden: If the Court please, I think that is an improper question. It calls for a conclusion of the witness on a point that seems to me to be one of law, as to the legal effect of a stockholder.

The Court: Objection sustained.

(Testimony of William H. Simon.)

By Mr. Webster:

Q. Mr. Simon, have you discussed this difference between your position as a stockholder and your position as a lender with your brother Mike Lyman? A. Many times.

Q. In the past it has been stipulated, that is, we have agreed that in the past you and your brother have gone into restaurant ventures in which you have used the form of [62] investing a portion of your money for the purchase of stock and of lending additional money for which you received back promissory notes.

Can you state whether the reason that you went into those deals on that basis was this distinction you had in your mind, which you are talking about?

A. You see, if we loan part of the money to a corporation if anything should happen to that corporation, where it would go broke, then we become a creditor and we get some of that money back as a creditor. If it is stock we just lose our money. We don't have any chance of recovery.

Q. Mr. Simon, did you participate in the formation of Wilshire and Western Sandwiches, Inc.?

A. I did.

Q. When was this deal first talked about?

A. It was in the early part of '41.

Q. Can you relate the circumstances surrounding the original discussions about the drive-in at Wilshire and Western?

A. You mean relative to Carpenter's across the street?

(Testimony of William H. Simon.)

Q. Yes, that is right.

A. Carpenter was operating a drive-in just a block away. It was a pretty old out-moded drive-in. At that time we were figuring on going in with Carpenter and moving the drive-in to the corner of Wilshire and Western, a block [63] up.

As a matter of fact, a lease was negotiated where the landlord was going to spend some seventy-five thousand dollars on the combination drive-in and restaurant and cocktail room. Right before the lease was to be signed Carpenter didn't feel he wanted to operate a combination restaurant. He thought it was a little too big for him. In the meantime I negotiated for the corner of Western and Wilshire, the other corner—what is that, the northwest corner?

Q. That is, the location of the present taxpayer?

A. The present drive-in, yes.

Q. All right.

A. I was going to put a drive-in on that particular corner and Carpenter asked me to let him put a drive-in on that particular corner and forego the other proposition, on account of it being too big.

Q. Now, Mr. Simon, the corporation in question, that is, Wilshire and Western Sandwiches, Inc., was incorporated in March of 1941. It is also stipulated that you signed a lease on this property which you are just talking about.

A. That is right.

Q. In April of 1941?

A. That is right.

Q. Was it your understanding then that the lease would be assigned over to the corporation?

(Testimony of William H. Simon.)

A. Yes.

Q. What was your understanding with respect to who would supervise the construction of the drive-in and operate it?

A. Harry Carpenter.

Q. Did you have any discussions with respect to the capital structure of the corporation?

A. Yes, we did.

Q. When was the first time you spoke about it?

A. Along about April, I should imagine, when we discussed Harry Carpenter taking that particular corner and me assigning the lease to Harry Carpenter.

Q. Who was present at the time of those discussions?

A. There was Harry Carpenter and my brother, Mike Lyman, and M. A. McDonnell.

Q. And yourself? A. And myself.

Q. What was the nature of that agreement or what was the nature of your discussion?

A. We discussed what we thought the costs would run on that particular drive-in, and we thought it would run around \$30,000.00.

At that particular meeting we further discussed that we would invest 50 per cent in stock and make a loan at 50 per cent. [65]

Q. Are you speaking about a formal board of directors' meeting? A. No, informal.

Q. The actual cost was greater or less than your estimate? A. Almost twice as much.

Q. Mr. Simon, with respect to this particular

(Testimony of William H. Simon.)

transaction involving Wilshire and Western, did you have any active part with respect to this decision you have just spoken about going in on a part loan-part stock basis? A. Yes.

Q. What was in your mind at the time?

A. I had other commitments for other restaurants, and I didn't want to freeze all my money in one particular unit. I just wanted to invest about 50 per cent and wanted loans for the other 50 per cent, as I stated before. I could always get my money back if the restaurant wasn't a success, out of depreciation. Then I was a minority stockholder and if I made a full investment I would have to depend on the other stockholders voting a dividend. I didn't want to put myself in that position.

Q. Do you know how much money was paid in by yourself, Mr. Lyman, Mr. McDonnell and Mr. Carpenter during the year 1941?

A. I think it was—I think we paid in \$30,000.00 as [66] an investment and \$25,000.00 as a loan.

Q. What was the total amount that went in?

A. \$55,000.00.

Q. What was the manner in which the corporation evidenced the receipt of this \$55,000.00? Do you understand what I mean?

A. No, I don't quite understand what you are asking.

Q. Did the corporation give you any documents of any kind which evidenced the receipt of money from you? A. No.

Q. Did you receive any stock certificates?

(Testimony of William H. Simon.)

A. No, not at that time. You mean after it was over?

Q. Well, I was speaking—apparently we are not together on the date at which we are speaking.

A. No.

Q. I was talking about the entire year 1941. You have testified that a total of \$55,000 was advanced.

A. That is right.

Q. I asked you whether the corporation issued any kind of documents to either you alone or to all four.

A. Yes, they did. Along about the fall of '41 they issued stock for my 50 per cent that I invested, and give me notes for the 50 per cent representing the loan.

Q. Do you remember how much in stock was given to you?

A. I think I got 500 shares and Mr. Lyman got 500 [67] shares.

Q. Mr. Simon, I show you what purports to be a promissory note of Wilshire and Western Sandwiches, Inc., in the amount of \$4,166.67, dated November 13, 1941. Do you recognize this?

A. Yes.

Q. What was your understanding when you received this note?

A. That it was to be paid back as a loan.

Q. Did this represent in your mind—

A. The moneys I put in.

Q. The moneys you put in? A. As a loan.

Q. What was your intent with respect to the \$4,166.67?

(Testimony of William H. Simon.)

A. That was a loan, I loaned the corporation that.

Mr. Webster: I would like to hand this for marking as Petitioner's exhibit next in order for identification.

Mr. Maiden: I have no objection to its being offered in evidence at this time, if counsel wants to offer it.

Mr. Webster: I do, your Honor.

The Clerk: 11.

The Court: 11, you say?

The Clerk: Yes, your Honor, please.

The Court: Let the instrument just identified by [68] the witness be admitted in evidence as the Petitioner's Exhibit No. 11.

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 11.)

By Mr. Webster:

Q. Now, it has been stipulated that of the total moneys which you advanced and that total it has been stipulated is \$9,166.67, a portion of it went in in May or thereabouts of 1941, and some more of it went in later, and a final amount went in in November.

Can you state what your intent was at the time that each of these payments was made?

A. Well, I just took it for granted that 50 per cent was an investment and 50 per cent was a loan.

Q. Did you have in mind exactly 50 per cent, Mr. Simon?

A. At the time we did, yes.

(Testimony of William H. Simon.)

Q. When did the drive-in open at Wilshire and Western? A. Some time in November.

Q. Early or latter part?

A. The early part of November.

Q. When was the decision made as to the amount which would be represented by stock and the amount which would be represented by notes?

A. The final decision?

Q. Yes. [69]

A. I think we had a stockholders' meeting just about that time, or maybe a little after the place opened up; just shortly after.

Q. Pardon me?

A. Shortly after the place opened up.

Q. Who was present at that meeting?

A. Mr. Carpenter, Mr. Lyman, Mr. McDonnell and Mr. Odell, the attorney, and myself.

Q. Where was that meeting held?

A. In my office at 649 South Olive Street.

Q. Mr. Simon, I show you a page titled "Written Consent and Waiver of Notice of Directors' Meeting" which is dated November 13, 1941, and which has on it five signatures. I ask you whether any of these signatures are yours.

A. There is my signature (indicating).

Q. That is your signature? A. Yes.

Q. Do you recollect seeing the pages which are attached to this waiver of notice?

A. Yes, I do.

Q. When did you see those?

A. Well, it was at my office some time in November.

(Testimony of William H. Simon.)

Q. Was it at the time of this meeting about which you are speaking? A. Yes. [70]

Q. These pages which are attached to this written consent and waiver of notice are titled "Minutes of Meeting of Board of Directors of Wilshire and Western Sandwiches, Inc."

These are the pages which were attached (indicating)? A. Yes.

Q. Were these pages prepared at the time you had that meeting? A. Yes, they were.

Q. Who prepared them?

A. Mr. Odell, the attorney.

Q. Do you know under what circumstances these pages were prepared? A. No, I don't.

Q. Are you aware of the contents of these minutes?

A. Several days before this meeting was called in my office I talked to Mr. Carpenter in regard to giving up part of my interest or making a gift of part of my interest and a part of Mr. Lyman's interest to Joe Lerdemer, my general manager. Mr. Lyman and myself, we each gave him 5 per cent of our stock as a gift.

Q. Mr. Simon, I will read a portion of these minutes to you and ask you whether you recall reading this before:

"He—" and the "he" referred to is Mr. Carpenter, the treasurer—"stated that the issuance of this permit [71] had been heretofore brought to the attention of the directors individually and that up to this time the following persons had agreed to take and pay for stock as follows:

(Testimony of William H. Simon.)

“Harry B. Carpenter, 1000 shares, \$10,000.00.

“M. A. McDonnell, 1000 shares, \$10,000.00.

“William H. Simon, 50 shares, \$5,000.00.

“Mike Lyman, 500 shares, \$5,000.00.

“It was further reported that the total cost of said building and equipment and of the improvement of grounds and accessories, in connection with said drive-in sandwich stand, would be in excess of \$55,000.00 and that pursuant to the understanding and agreement between said corporation and said Carpenter, McDonnell, Simon and Lyman, said persons had loaned to said corporation \$25,000.00 in the following proportions:

“Harry B. Carpenter, \$8,333.34.

“M. A. McDonnell, \$8,333.33.

“William H. Simon, \$4,166.67.

“Mike Lyman, \$4,166.66.”

I ask you whether the contents of these minutes, as I have read them now, was a matter which you read yourself previously? A. Yes. [72]

Q. You read those at the meeting which you spoke about? A. That is right.

Q. Which occurred in your office?

A. Yes.

The Court: Don't lead your witness.

Mr. Maiden: Does counsel want to offer that in evidence?

Mr. Webster: Yes.

Mr. Maiden: I have no objection, if the Court please.

The Court: Proceed.

(Testimony of William H. Simon.)

The Clerk: Exhibit 12.

The Court: The minutes, papers attached thereto, identified by the witness, are admitted in evidence as Petitioner's Exhibit No. 12.

(The documents above-referred to were received in evidence and marked Petitioner's Exhibit No. 12.)

By Mr. Webster:

Q. Mr. Simon, did the conversation which you had with Mr. Carpenter a few days previously discuss at all the contents of these minutes?

A. There was something discussed; the general construction of the whole thing, yes.

Q. Did you speak at all about issuing \$30,000.00 of stock? A. No, I don't think so. [73]

Q. You don't remember?

A. I don't remember.

The Court: Don't lead your witness. Your witness said he didn't think so. You prompted him to say he didn't remember. You are going to hurt your own witness and your own case by leading in such a way.

By Mr. Webster:

Q. Mr. Simon, did you ever receive a stock certificate of Wilshire and Western?

A. Yes, I did.

Q. Can you recall when you received it?

A. It was some time in the latter part of November.

Q. Was that the only certificate which you ever received?

(Testimony of William H. Simon.)

A. No. I received one earlier, but then we changed the amount of shares that Mr. Lyman and myself were going to get by giving Mr. Lerdemer a gift of 5 per cent apiece.

Q. Where is the stock certificate which you received? A. In my safety deposit vault.

Q. Has Mr. Lyman received a stock from Wilshire and Western? A. Yes, he has.

Q. Can you describe the circumstances under which he received the stock certificate?

Mr. Maiden: If the Court please, I object to that. [74] I think it would be hearsay. I think Mr. Lyman himself out to testify whether he received any stock and when he received it.

The Court: This witness might have seen it. It wouldn't be hearsay. He is not asking for what was said.

The Witness: It is not hearsay, your Honor.

The Court: Just answer the question. We will pass upon the question, as to whether it is hearsay or not.

The Witness: Yes, I received it from Mr. Lyman.

The Court: Proceed with your examination. The objection is overruled.

The Witness: I received it from Mr. Lyman.
By Mr. Webster:

Q. I didn't hear your answer.

A. I received the stock from Mr. Lyman.

Q. Mr. Simon, can you state whether you intended to purchase stock in Wilshire and Western?

(Testimony of William H. Simon.)

Mr. Maiden: That is a leading question. I object to it.

The Court: In that form it is leading, yes. The objection will be sustained.

By Mr. Webster:

Q. Mr. Simon, when you received the note which has been introduced as Petitioner's Exhibit 11, did you expect that that note would be repaid? [75]

A. I certainly did.

Q. When?

A. I think it was two years from the date.

Q. Mr. Simon, how did you receive the stock and note, did somebody hand it to you, or how did you receive it?

A. Just gave it to me. I was sitting at my desk and they just gave me the stock and a note.

Q. Did you receive the stock and note at the time of the meeting, that you recall?

A. I don't remember.

Q. Can you fix a time when you received the stock and note?

A. I think it was some time in November, the latter part of November.

Q. Mr. Simon, it has been stipulated that on April 21, 1943, a check was issued to you by Wilshire and Western in the amount of \$1,666.16, and that in the voucher portion of the check, that is, in the upper left-hand side was the statement, "Payment on Note." Do you recall receipt of this check? A. Yes, I do.

Q. What did you understand at the time of receipt?

(Testimony of William H. Simon.)

A. It was a repayment on the note, on the loan.

Q. On May 23, 1944, it has been stipulated that you received a check for \$1,667.17, which bore a notation in the [76] voucher portion of that check, that is in the upper left-hand corner, "Note Accounts." Do you remember receiving that check?

A. Yes.

Q. What was your understanding?

A. Repayment of the loan.

Q. It has been stipulated on March 23, 1945, a check for \$833.34 was issued to you marked in the voucher portion of the check, "Balance on Note." Do you remember receiving that check?

A. Yes, I do.

Q. What was your understanding?

A. As a repayment of the loan.

Q. Mr. Simon, I show you a check numbered 2046 bearing the imprint at the lower right-hand corner, "Wilshire and Western Sandwiches, Inc." It is made out to you, dated December 1, 1943, and is in the amount of \$509.31. In the upper left-hand corner is the notation, "Interest to November 3rd inclusive." Do you recall receiving that note?

A. Yes.

Q. What was your understanding at the time?

A. It was interest on the loan.

Mr. Webster: I would like to offer this check as Petitioner's exhibit next in order. [77]

Mr. Maiden: No objection, if the Court please.

The Clerk: Exhibit 13.

The Court: Petitioner's Exhibit 13 is admitted in evidence, being the check just identified by the witness.

(Testimony of William H. Simon.)

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 13.)

By Mr. Webster:

Q. I show you Check No. 4136, bearing the imprint in the lower right-hand corner, "Wilshire and Western Sandwiches, Inc." It is made out to William Simon in the amount of \$113.68. It bears in the upper left-hand corner "Interest on Note to March 24th." Do you remember that check?

A. Yes, I do.

Q. Do you remember receiving it?

A. I do.

Q. What was your understanding at the time of receipt? A. It was interest on the loan.

Mr. Webster: I offer this as Petitioner's exhibit next in order.

The Clerk: 14.

The Court: Petitioner's Exhibit 14 is admitted in evidence.

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 14.) [78]

Q. Do you remember any other interest payment? A. I don't remember.

Q. Did you pay anything further into Wilshire and Western Corporation over and above the amounts which we have already talked about?

A. Yes, we did.

Q. When?

A. It was after the place was opened, Carpen-

(Testimony of William H. Simon.)

ter told us that he needed some additional \$10,000.00 to pay all the remaining bills outstanding.

Q. Can you recall more accurately when that was?

A. I imagine it must have been toward the end of November.

Q. Do you identify it as the time when you received the note and stock?

A. No, it was after we received the note and stock.

Q. How long afterwards?

A. Oh, maybe a couple of weeks afterwards; maybe longer. Maybe the first part of December.

Q. Did Mr. Carpenter ask you for any money?

A. Yes, he did.

Q. Do you remember how much?

A. I think if my memory serves me between my brother and myself we put up around a third of \$10,000.00.

Q. And yourself?

A. Half of that amount. [79]

Q. Half of a third? A. Yes.

Q. What did Mr. Carpenter tell you with respect to this money which he asked you for?

A. Well, he says, to loan the corporation this money and he could pay it back in a short time, not to take any notes for it at that time.

Q. Did you expect any interest on that transaction.

A. No, because it was going to be paid back.

Q. Mr. Simon, I show you Check No. 792 bearing the imprint in the lower right-hand corner,

(Testimony of William H. Simon.)

“Wilshire and Western Sandwiches, Inc.” made out to William Simon in the amount of \$1,666.67. In the upper left-hand corner it has the description, “Note Account.”

I ask you if you remember this check.

A. Yes.

Q. Did you receive it? A. Yes.

Q. What was your understanding?

A. Repayment of loan.

Q. Which loan was it a repayment of?

A. Of that last \$10,000.00.

Mr. Webster: I offer this check as Petitioner's exhibit next in order.

Mr. Maiden: If the Court please, it just occurred [80] to me we have been wasting time and we needn't carry this procedure further, because at page 6 of our stipulation we have stipulated on the following dates checks of the Petitioner were issued and delivered to the following named persons in the amounts indicated, with an explanation in the voucher portion of each check as follows, and then it lists each of the charges and the payee.

Mr. Webster: Your Honor, that is certainly true, but there is nothing in the stipulation about the understanding of the recipient of these checks.

The Court: You could at least, considering the state of your stipulation, take the stipulation and ask him his intent on each of these, without putting them in evidence, without taking that much time.

You have agreed that these checks were issued and delivered, each of them. In other words, you

(Testimony of William H. Simon.)

have here about as sufficient a description of each of these checks as you can, I take it.

Mr. Webster: If I may interrupt, I believe counsel for Respondent has made an error. I have not introduced into evidence a single one of these checks set out on page 7, if those are the checks he is speaking of at the moment.

Mr. Maiden: It is my point, your Honor, that is true.

The Court: I was taking you at your word.

Mr. Maiden: Yes, I made a mistake.

The Court: We will be recessed at this time for 10 minutes.

The Clerk: The last exhibit number is 15.

The Court: Exhibit 15 will be admitted in evidence.

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 15.)

(Short recess taken.)

By Mr. Webster:

Q. Mr. Simon, in previous deals have you ever used bank loans? A. Yes, sure.

Q. Have you used and are you familiar with doing business with a bank? A. Yes, I am.

Q. Did any discussion ever take place with respect to borrowing from a bank for this transaction?

A. Well, there was some discussion about going to the bank and borrowing this money, and I felt that it was a good loan and paid 6 per cent and

(Testimony of William H. Simon.)

I thought we could use that 6 per cent as well as the bank.

Q. Do you know anything about the books of Wilshire and Western Sandwiches, Inc?

A. No, I don't.

Mr. Webster: That is all. [82]

The Court: Cross examination.

Cross Examination

By Mr. Maiden:

Q. Mr. Simon, I believe the stipulation of facts in the case shows that this Petitioner was incorporated on March 24, 1941. I believe you stated that prior to that time you had discussed with Mr. Carpenter the formation of this corporation for the purpose of building a drive-in restaurant upon some property that you either had leased at the time or intended to lease, is that right?

A. That is right.

Q. I believe the stipulation shows that a lease was to be taken by you on the 26th day of April, 1941. And I believe you testified that it was your intention at the time of obtaining this lease to assign the lease to the corporation.

A. That is right.

Q. It was your understanding that the corporation would then assume, under the lease, the obligations that you yourself had assumed?

A. That is right.

Q. Now, Mr. Simon, I believe you stated that you had been in the restaurant business for some 25 or 30 years.

A. Yes.

(Testimony of William H. Simon.)

Q. During that time did you operate drive-in [83] restaurants all the time or a different type of restaurant?

A. No, we have only operated drive-in restaurants since 1935.

Q. Briefly, what is a drive-in restaurant?

A. Well, a drive-in restaurant is a restaurant that an automobile drives on the lot and you serve the customer in the car.

Q. Now, the stipulation shows that in February of 1941 a corporation by the name of Symon's Beverly, Inc. commenced business and that William H. Simon was one of the stockholders in that corporation. That is correct, is it not?

A. That is correct.

Q. The stipulation likewise sets forth the fact that in November of 1941 Simon's Florat, Inc. commenced business and William H. Simon was one of the Stockholders, is that true?

A. That is true.

Q. And William H. Simon is yourself?

A. Yes, sir.

Q. The stipulation further shows that Simon's Five Points, Inc. commenced business on November 1, 1941, and that William H. Simon was a stockholder. That is correct?

A. That is correct.

Q. And that on September 23, 1941, Simon's Washington, [84] Inc. commenced business and that William H. Simon was a stockholder, is that correct?

A. That is correct.

Q. And that Sunset Sandwiches, Inc. com-

(Testimony of William H. Simon.)

menced business on January 29, 1941, and that William H. Simon was a stockholder, that is correct?

A. That is correct.

Q. Now, Mr. Simon, when this corporation was set up and a certificate of incorporation was issued to it, you knew at that time that you would be going to build a drive-in restaurant upon this leased property?

A. Will you repeat that question, please?

Q. I say, at the time this corporation received its certificate of incorporation—

A. You mean from the Corporation Commissioner?

Q. —at the time it was incorporated.

A. Yes.

Q. You knew that the corporation would build a drive-in restaurant upon that leased property?

A. That is right.

Q. How much did you estimate at that time the cost of building the drive-in restaurant building would amount to?

A. We figured it would cost about \$30,000.00 for the building and equipment.

Q. How much did you estimate the building by itself [85] would cost you, Mr. Simon?

A. It usually ran about half for the building and half for the equipment.

Q. In other words, you expected at the time of the incorporation of the business that it would cost you approximately \$15,000.00 for the building and approximately \$15,000.00 for the equipment.

A. That is right.

(Testimony of William H. Simon.)

Q. Those two items being essential to the commencement of the business you intended to carry on.

A. That is correct.

Q. Now, I believe, Mr. Simon, that according to the stipulation the Articles of Incorporation authorized capital stock of 7500 shares of common stock of a par value of \$10.00 per share.

I wonder if you provided for the issuance of 7500 shares at \$10.00 a share, which would be \$75,000.00?

A. I really don't know. I can't answer that.

Q. Would you say it was your intention at that time to invest \$75,000.00 in this business?

A. No, possibly—

Q. If it became necessary.

A. Possibly not.

Q. Was that just some figure you pulled out of the air, 7500? [86]

A. I can't answer that question.

Q. Now, the stipulation shows that on July 10, 1941, a building construction contract was entered into between this Petitioner and Frank A. Woodyard, under which Mr. Woodyard contracted to construct a drive-in building for the sum of \$22,651.00. That would indicate that as of July 10, 1941, you knew that the building alone would cost you a minimum of \$22,651.00, isn't that correct?

A. That is correct.

Q. And at that time, I believe, from your direct examination no shares of stock had been issued by the corporation?

A. That is correct.

Q. Then wasn't it apparent to you stockholders

(Testimony of William H. Simon.)

or incorporators on July 10, 1941, that the corporation would have to have at least \$37,651.00 in order to build its building and equip it for business, is that correct?

A. No, I don't know whether it is or not. If you say that building contract was twenty two thousand some odd dollars, it would cost more than \$37,000.00, the way I figure the thing. It would cost 50 per cent for building and 50 per cent for equipment.

Q. In other words, as of July 10, 1941, since your building contract called for \$22,651.00, you knew that your equipment would cost approximately the same amount, is that [87] right?

A. That is right.

Q. Now, the stipulation in this case further shows that on July 14, 1941, an application was filed with the Corporation Commissioner to permit the sale, the issuance and sale of the Petitioner's stock to yourself and your brother, Mike Lyman. Is he your brother?

A. Yes, sir.

Q. And Mr. Harry B. Carpenter and M. A. McDonnell and Harry B. Carpenter Jr. And that you asked at the time for permission to sell for cash \$15,000.00 worth of this stock or 1500 shares.

And you further asked permission to issue additional shares for the purpose, if necessary, of furnishing the corporation sufficient money to complete its drive-in building and equip it for opening business.

Now, Mr. Simon, how much money did you intend to invest in this corporation?

(Testimony of William H. Simon.)

A. Originally we intended to invest, the group, \$15,000.00 and loan \$15,000.00.

As we progressed we intended to advance this money on the same ratio of 50 per cent investment and 50 per cent loan.

Q. Well, you intended or thought at least that you might issue sufficient stock for cash to pay the entire cost of building the drive-in restaurant building and equip it for business, isn't that true?

A. No, I don't think so. I don't think that was ever true.

Q. Do you realize that such a provision as that is actually in the application which you filed with the Corporation Commissioner for issuance of stock?

A. I don't remember.

Q. If such a provision as that is in the application, you don't deny its veracity?

A. I beg your pardon?

Q. If such a provision as that is in the application, then, of course, you don't deny it?

A. I don't know. I don't run my business. I know what my intentions were and I don't—I am not a lawyer, I don't go over stock applications and books. I am not a lawyer nor an auditor. You might be right. I don't know whether you are not. I know what my intentions were at the time and that is all I can testify to.

Q. Now, Mr. Simon, the stipulation shows that between June 9, 1941, and November 13, 1941, that you and Mr. Lyman had advanced certain money to the corporation. Now, will you please explain to the Court why it is that in return for the money

(Testimony of William H. Simon.)

advanced by you you took capital stock for only half the amount and instruments in the [89] form of promissory notes for the other half?

A. At the start of this particular proposition, when we had an informal meeting, it was agreed at that time that we would invest 50 per cent and take 50 per cent in notes as loans. As I testified earlier, I didn't want to freeze too much money in that particular unit. I had other commitments and I didn't want to come in there just as a stockholder, I wanted to come in there partially as a stockholder and partially as a creditor. One, I could get my money back faster even if the place wasn't a success. I didn't have to wait for dividends to be earned to get my money back that way. I could get it back out of the depreciation.

No. 2, if the place would fail, I became a common creditor.

Q. What do you mean by getting your money out of depreciation?

A. As a loan, when it was set up as a loan, the place didn't have to make a loan—money to meet the loan every month and they depreciate the place over a 10-year period. If the place didn't make money there was enough money from depreciation to pay back those loans.

Q. Do you mean the company set up a cash reserve each month for depreciation?

A. Every corporation depreciates their investment.

Q. Did this corporation actually set aside and earmark [90] cash money for depreciation?

(Testimony of William H. Simon.)

A. According to the law, as I understand it, the tax law, you can depreciate 90 per cent of your investment to be depreciated over a period of 10 years. If you have a 10-year lease you can depreciate it over a period of 10 years. You can depreciate that monthly.

Q. How was that going to return your cash money to you, is what I don't understand, Mr. Simon.

A. Well, as the investment is depreciated that money accumulates.

Q. How did you expect to be repaid for these loans, except out of the current earnings of the business?

A. You don't have to have current earnings to be paid back on a loan.

Q. How would the corporation pay you back on the loan if it did not make any money?

A. You have a depreciation account they could use. You are depreciating your investment.

Q. What was the cost of the building? I believe the stipulation shows that. \$40,489.68.

Suppose the corporation didn't make sufficient money to set up a depreciation reserve, how then did you expect to get the return of cash money from your loan?

A. You mean if they lost money?

Q. Yes. [91]

A. If they lost beyond their depreciation account, well, I would just have to come in as a creditor.

Q. In other words, this corporation, you had to

(Testimony of William H. Simon.)

realize this corporation had to make money before you could expect the payment back of your loan?

A. No, I didn't realize that. I don't know that. I don't think that is a bit necessary.

Q. Well, suppose the corporation hadn't made any money.

A. And if they didn't lose any money?

Q. Suppose they didn't make any money and actually lost money.

A. Well, that would be too bad. I would lose my money.

Q. In other words, you knew that your loan was just as good as the company's ability to make money, is that right?

A. That is right.

Q. Now, what difference actually would it make to you, Mr. Simon, whether or not you had your entire advancement in capital stock rather than part in capital stock and part in a loan?

A. I explained that. I didn't want to freeze my money, the whole amount, as an investment. The restaurant business is a very hazardous business and I wanted to protect my money. I only wanted 50 per cent in stock and I wanted to [92] make a loan of the other 50 per cent, so if the place did go broke I would become a creditor and I would recover some of my money. If I was a stockholder I would lose it all.

Q. Now, Mr. Simon, since you say the restaurant was such a hazardous business, why were you willing to risk your own cash money in addition to the amount you say you were willing to subscribe for stock?

(Testimony of William H. Simon.)

A. You mean after the place was opened?

Q. Yes. A. The last \$10,000.00?

Q. No. I am talking about the amount of money you advanced to the corporation.

A. You mean the 50 per cent?

Q. Yes. A. I am used to gambling.

Q. I believe you stated you didn't want to go to the bank and get the money because you felt like you thought it would make money.

A. That is right.

Q. A safe loan.

A. That is right. I wanted that 6 per cent.

Q. You wanted that 6 per cent. Now, Mr. Simon, I am going to ask you a direct question and I would appreciate a direct answer. Was this arrangement conceived and carried through for the purpose of being able to get a return of a [93] portion of the money advanced to this corporation, without having to pay any tax on it and in order to allow the corporation to take a deduction out of current earnings for interest?

A. Positively not.

Q. Mr. Simon, did you take into consideration the tax benefits that would be derived by you and the corporation by treating part of this money as a loan, rather than as an investment?

A. I would say yes.

Q. So then the tax benefit was taken into consideration in this arrangement?

A. No, no, not wholly.

Q. You said that it was considered.

A. You asked me a direct question and I an-

(Testimony of William H. Simon.)

swered you direct. Then you asked me another question and I answered you. No.

Q. Well now, you stated that that was the tax benefit that was taken into consideration.

A. You asked me if I knew whether there was a tax benefit, sir, and I said I did. Then you asked me a question whether I took that into consideration at the outside, when we discussed this proposition, and I says no. It was a policy that we pursued.

Q. In other words, you knew that there was a tax [94] benefit to be derived by you and the corporation, but you deny that that knowledge in any way influenced this arrangement.

A. That is right, sir.

Q. In other words, you weren't interested in obtaining any tax benefit.

A. At the time I was only interested in protecting my capital.

Q. Now, Mr. Simon, the stipulation shows that you incorporators advanced \$55,000.00 to the corporation prior to its commencement, actual commencement of business. Was that \$55,000.00 an essential expenditure in order to permit this Petitioner to open for business? A. Yes.

Mr. Webster: May I interrupt, your Honor? I would like that question read.

The Court: Read the question.

(The question was read.)

Q. (By Mr. Maiden): Now, Mr. Simon, I want to call your attention to page 9 of the stipulation that we have entered into, and just for your

(Testimony of William H. Simon.)

benefit to yet you see exactly what I am talking about, I want to read you this Paragraph 16 which says, "The stockholders of Petitioner, or some of them, have entered into similar transactions wherein they advanced money to [95] other corporations for a portion of which they received capital stock thereof and for the balance of which they received documents designated 'promissory notes'" and then it gives a list of some nine such corporations. I call your attention to the M & S Foods, Inc., which shows that the stockholders received \$36,000.00 in stock and received instruments designated promissory notes in the amount of \$108,000.00. What is your explanation for that situation?

A. I can't give you any explanation of it.

Q. Can you tell the Court why it is in all of these other corporations of which you were an incorporator and stockholder that the advancements made to the corporation were discharged by the corporation by issuance partially of stock and the balance in notes?

A. I couldn't go into those things intelligently at the present time.

Q. Was the arrangement in these other corporations prompted by the same motive you had in the instant case?

A. I can't answer that intelligently, sir.

Q. How can you answer it?

A. I can't answer it at all.

Q. In other words, you have no explanation to offer as to why in all these other corporations this same arrangement was put into effect?

(Testimony of William H. Simon.)

A. I wouldn't care to answer. I couldn't give you [96] an intelligent answer at the present time.

Q. Now, Mr. Simon, I call your attention to Petitioner's Exhibit 11 which has been identified as a note given to you by this Petitioner, in return for \$4,166.67 of the total advance made by you to the Petitioner. Was it your intention at the time this note was executed to demand payment of that note at its due date, regardless of the financial condition of the corporation at the time?

A. That is right.

Q. It was? A. Yes, sir.

Q. Even though it meant the liquidation of the business?

A. I don't suppose so. I would be very fair about it.

Q. In other words, you would not have insisted upon the payment of this note at its due date if it meant a financial hardship to the business?

A. No, I don't suppose I would.

Q. It was your intention or thought that you would receive payment of this note out of the current earnings of the business?

A. Yes, sir.

Q. There wasn't any question of you and the other gentlemen interested in this corporation not having enough cash money to pay the costs incident to the opening of the business? [97]

A. Well, I can only answer that for myself, sir.

Q. Well? A. I had money.

Q. You had plenty? A. Yes, sir.

(Testimony of William H. Simon.)

Q. Could you have financed the entire opening cost of this business, if necessary?

A. I don't think so, not at that time.

Q. But you could have purchased the four thousand odd dollars shown on that note in shares of stock of the company, isn't that right?

A. I think the record show that, sir.

Q. Can you explain to the Court why it was, Mr. Simon, that the notes issued by this corporation were in direct proportion to the shares of stock issued by the corporation?

A. Well, originally when we had this informal meeting we arbitrarily thought that was a fair division, 50-50.

Q. I believe you stated that you don't know anything about the books of the corporation.

A. That is right, I do not, sir.

Q. Did you sign any income tax return for the corporation?

A. I don't think I ever did, no; at least. I don't think so.

Q. In these other corporations that are set out in the [98] stipulation, which I have called to your attention, did you hold any official position with any of those corporations? F & LB Corporation?

A. I might be an officer in this corporation (indicating).

Q. Were you a member of the board of directors? A. I think so.

Q. What about F & S Foods, Inc.?

A. I think so.

(Testimony of William H. Simon.)

Q. A member of the board of directors and an officer? A. Yes.

Q. What about Carsim, Inc.?

A. I think I am president there.

Q. I will ask you to look at the other corporations and state whether or not you were an officer and member of the board of directors.

A. Officer (indicating); officer (indicating); officer (indicating); officer (indicating); nothing there, I don't think (indicating).

Q. You were not an officer of Sunset Sandwiches, Inc.? A. No.

Q. Were you a member of the board of directors?

A. I don't think so. I don't know. I can't tell you for sure. I had nothing to do with that.

Q. You had nothing to do with Carleton's, Inc.?

A. No, sir.

Q. But you stated on direct examination, I believe, that one reason why you wanted part of your advances to be treated as loans was because you were a minority stockholder and you were afraid that dividends might not be declared often enough to suit you, is that right?

A. Well, being a minority stockholder I had no control over that corporation.

Q. You were in business with the majority stockholders in this corporation, in these other corporations that we talked about, weren't you?

A. Some of them, yes.

Q. You and Mr. McDonnell and Mr. Carpenter

(Testimony of William H. Simon.)

and the other gentleman named in these other corporations, I take it, are close personal friends.

A. Yes, sir.

Mr. Maiden: I believe that is all, if the Court please.

The Court: Are there any further questions?

Mr. Webster: Yes, your Honor.

Redirect Examination

By Mr. Webster:

Q. Mr. Simon, with respect to the corporations whose names appear in the stipulation at pages 8 and 9, which was shown to you previously by Mr. Maiden, this stipulation shows [100] that capital structure of each of those corporations was represented in part in the form of stock and in part in the form of notes. I am addressing my question now not to the actual division in dollars between stock and loans, I am simply addressing my question now to the fact there was a division in the first place between stock on the one hand and loans on the other.

A. That is right.

Q. I ask you whether you know what the reason for that division was.

A. Well, I imagine it would carry through for the same reason——

Mr. Maiden: Your Honor, I believe the witness stated on direct examination he couldn't answer such a question as that intelligently, and he didn't care to make any statement about it.

Mr. Shearer: The question, if your Honor

(Testimony of William H. Simon.)

please, on cross examination to which counsel refers, referred to specific figures.

Each question directed the witness' attention to whatever the amount of dollars was in stock and whatever the amount of dollars was in loans. That is not the same question as the question here presented, if your Honor please.

Mr. Maiden: I did ask him if he could explain why it was that the same arrangement was used in these other [101] corporations as was used in this instant case.

The Court: Read this present question.

(The question was read.)

The Court: I think it is true the question was asked the witness on direct examination and he stated he couldn't and didn't care to answer the question; he couldn't answer it intelligently. However, I am not going to sustain the objection. The objection is overruled. Proceed.

The Witness: Well, as I said, I imagine the same arrangement was carried through for the same reasons on these corporations as on this corporation in question here. [102]

By Mr. Webster:

Q. Mr. Simon, on cross examination you were asked as to why, in the case of Wilshire and Western Sandwiches, the loans were made in proportion to stockholdings. It is my understanding that your answer was not exactly directed to the question. Would you give us the answer now to that question?

(Testimony of William H. Simon.)

A. Well, it was at an informal meeting when we first contemplated this venture. We agreed on whatever moneys we put up, that fifty percent would go for stock as an investment and fifty percent toward a loan.

Q. Mr. Simon, I see where this misunderstanding possibly arises. I think what counsel for Respondent means was if you took one third of the stock, you and your brother took one third of the stock, did you make one third of the loans?

A. Yes, we did.

Q. Can you give a reason for why that took place?

A. I don't understand what—will you repeat that, please? I don't understand it.

Q. You and your brother together took thirty-three and a third percent of the stock. You made thirty-three and a third percent of the loans, and the question is this: Since you took one third of the stock and made one third of the loans and since Mr. Carpenter took one third of the [103] stock and made one third of the loans and Mr. McDonnell took one third of the stock and made one third of the loans, what was the reason for that kind of proportion?

A. Well, my brother and myself are always considered one unit.

Q. Mr. Simon, on cross examination you were asked as to whether the fact that as a minority stockholder you do not have control over the declaration of dividends was the reason for your going into this part loan-part stock setup?

(Testimony of William H. Simon.)

A. No, not wholly.

Q. That is what I wanted to know. Was that the sole reason? A. No, no, no.

Q. Mr. Simon, do you recall any instances when you had differences of opinion with Mr. Carpenter or Mr. McDonnell on business matters?

A. Nothing serious.

Mr. Webster: That is all, your Honor.

Mr. Maiden: No further questions, if the Court please.

The Court: I want to ask the witness one question.

By the Court:

Q. I have before me here in this stipulation, Mr. Witness, a list of corporations, other corporations about which you have been asked. I merely wanted to ask you [104] whether you were a majority stockholder in any of those. A. No, sir.

Q. Were you a minority stockholder in each of them? A. Yes, sir.

Q. I will ask you this further: Were you and your brother together—you spoke of your brother and you being a unit in these matters—were you and your brother, taken together as a unit, always in the minority in these corporations?

A. In the Simon corporations we were in the majority.

Q. Which one was that?

A. Simon's Florat, Simon's Washington, Simon's Five Points.

(Testimony of William H. Simon.)

Q. These with the word "Simon's" in the title of the corporation, you were in the majority?

A. Yes, sir.

Q. When you were in the majority, you put your name in the corporation, is that right?

A. Yes.

Q. When you and your brother were in the majority?

A. That is right, sir.

The Court: That is all I want to ask.

Mr. Maiden: I want to ask one further question, if I may.

The Court: Proceed. [105]

Recross Examination

By Mr. Maiden:

Q. Mr. Simon, I will ask you if it isn't a fact that in each of these corporations, other than the corporation that we are now trying in this matter and with the exception of Carleton's, Inc., wherein you do not appear to have been a stockholder, if the moneys advanced to these corporations were not the moneys needed by the corporations to pay for their buildings and equipment preparatory to opening for business.

A. I imagine.

Mr. Maiden: That is all, if the Court please.

Mr. Webster: That is all, your Honor.

The Court: This witness is being excused by both sides, is he?

Mr. Maiden: Yes, sir, so far as I am concerned.

Mr. Webster: Yes, your Honor.

The Court: You are excused from further attendance.

(Witness excused.)

The Court: Before you start interrogating the next witness, let me inquire in a general way how much longer you expect to take. I am not hurrying you, but I want to get a general idea of how much longer you expect to take.

Mr. Webster: I imagine on direct about two hours.

The Court: Proceed. [106]

Whereupon,

HARRY B. CARPENTER

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Clerk: Tell us your name, sir.

The Witness: Harry B. Carpenter

Direct Examination

By Mr. Webster:

Q. Mr. Carpenter, you are in the restaurant business? A. Yes.

The Court: It might be of some convenience to some of your witnesses to say I shall not sit more than a few minutes after 5:00 o'clock. If you think you are going to take that much time for this witness, you may excuse the others.

Mr. Maiden: May I speak to one of my witnesses?

The Court: Yes.

Mr. Maiden: If the Court please, I have a request to make at this time of the Court and of counsel. I have present a witness who will not be available to me tomorrow. It would only take about 10 or 15 minutes for my direct examination of him. I would like to put him on now out of order.

The Court: What does the Petitioner say? [107]

Mr. Shearer: No objection.

Mr. Webster: That is all right.

The Court: Very well. Withdraw this witness, then, and put on the witness for the Respondent out of order.

(Witness withdrawn.)

The Court: If you are going to take 10 or 15 minutes, we might take some testimony from this witness later, although I think probably not. The other witnesses, besides the one that is going on the stand now and the gentleman who has just been on the stand, Mr. Carpenter, may be excused if they wish until 10:00 o'clock tomorrow morning.

Whereupon,

BENJAMIN H. WHITTAKER

called as a witness for and on behalf of the Respondent, having been first duly sworn, was examined and testified as follows:

The Clerk: Tell us your name.

The Witness: Benjamin H. Whittaker.

Direct Examination

By Mr. Maiden:

Q. What is your business, Mr. Whittaker?

A. Certified public accountant.

(Testimony of Benjamin H. Whittaker.)

Q. How long have you been a certified public accountant? A. About 25 years. [108]

Q. Where have you practiced your profession?

A. Since World War I, in Los Angeles.

Q. Mr. Whittaker, are you acquainted with Mr. Carpenter and Mr. Simon?

A. Not with Mr. Simon, but with Mr. Carpenter, yes.

Q. Was that the Mr. Carpenter who was just sworn in as a witness previous to your taking the stand? A. Same one.

Q. Have you ever heard of the Wilshire and Western Sandwiches, Inc., corporation?

A. I have.

Q. When did you first become acquainted with that corporation? A. In '41.

Q. Will you briefly state how you became acquainted with the corporation?

A. I was connected with Mr. Carpenter with his taxes. This new corporation was formed, and Mr. Carpenter came to my office and asked me to outline a set of records for his bookkeeper to install and use.

Q. Do you recall whether or not his first visit to you after this corporation had been formed?

A. Oh, yes, it was after.

Q. You say he came to you for the purpose of what?

A. Having a set of books outlined and set up to be [109] used for the corporation.

Q. What did you do, Mr. Whittaker?

A. I first of all asked Mr. Carpenter for a copy

(Testimony of Benjamin H. Whittaker.)

of the minute book, and so forth, which I received from Mr.— the attorney.

Q. In point of time, will you tell the Court when that was? A. Yes. It was in October.

Q. Of what year? A. 1941.

Q. Did you receive a copy of the minutes of the corporation?

A. The minute book itself was sent over to me by Mr.—

Q. Was it Mr. Odell?

A. Mr. Odell, yes, October 23rd. I asked him to deliver to my secretary the books of the Wilshire and Western Sandwiches, Inc., as per our telephone conversation, “and will return them to you shortly.” He sent them over.

Q. Will you briefly explain why it is you wanted the minutes of the corporation for the purpose of setting them up some books?

A. Because I wanted to prepare an opening journal entry, which would give the date of incorporation and the capital stock and how it was divided, and its permit from the Corporation Department, and who the first officers were, and [110] the question of a lease also came up.

Q. Now, then, did you prepare a set of books or just an outline as to how the books should be set up?

A. I sent them an index for the books and a copy of the opening journal entry, of what I had prepared there.

Q. Now, the outline or list of records that you

(Testimony of Benjamin H. Whittaker.)

sent the corporation, did it include an account for notes payable? A. It did.

Q. Did the opening journal entry that you sent them provide that the corporation was incorporated with a capital of \$75,000.00? A. It did.

Q. Divided into 7,500 common shares of \$10.00 each par value? A. That is correct.

Q. Did it likewise recite the fact that the company had received permission from the Corporation Commission to issue 7,500 shares of its common stock for cash to Harry B. Carpenter, M. A. McDonnell, William H. Simon, Mike Lyman, and G. C. Jobson? A. Or to any or all of them.

Q. At the time you examined those minutes, did you carefully read those minutes?

A. I wouldn't say that I scrutinized them closely. I looked through them for anything that might affect their [111] financial books.

Q. Now, Mr. Whittaker, did you keep the books of this corporation? A. No.

Q. Do you know who kept the books of the corporation?

A. A Mrs. Jennings, I think, is her name.

Q. She was an employee of the corporation?

A. She was an employee of the corporation, of Mr. Carpenter's; all of Mr. Carpenter's interests.

Q. Now, did you prepare the 1941 corporation income and excess profits tax return for this corporation?

A. The income, yes. There was no excess profits tax prepared.

(Testimony of Benjamin H. Whittaker.)

Q. Is this the 1941 return prepared by you, Mr. Whittaker (indicating)?

A. Yes, that is my signature.

Q. In preparing that return, what investigation did you make or have made of the books and records of the corporation for the year 1941?

A. I took a trial balance of the books.

Q. When was that trial balance taken, Mr. Whittaker, would you say?

A. Some time after the 15th of January, between that time and the 7th of March.

Q. 1942? [112] A. 1942.

Mr. Maiden: I believe this return for 1941, which is Joint Exhibit 8-H to the stipulation, if the Court please, shows that it was sworn to on the 11th day of March, 1942.

The Witness: Yes.

By Mr. Maiden:

Q. And was signed by you as the person preparing the return on the 11th day of March, 1942?

A. That is correct.

Q. Now, referring you to the return, does the balance sheet appearing on page 4 of this return—

A. Yes.

Q. —is that the same as the trial balance you had taken off the books? A. Yes.

Q. Of the corporation? A. It is.

Q. Now, will you explain what the books showed as of December 31, 1941, with respect to the capital structure of the corporation?

A. The books showed a capital stock of \$75,-

(Testimony of Benjamin H. Whittaker.)

000.00, of which \$55,000.00 had been set against an account which read "Cash Special \$55,000.00."

Q. Did the books as of December 31, 1941, show any notes payable to the stockholders? [113]

A. No.

Q. Now, this 1941 return, being Exhibit 8-H, shows the capital stock subscriptions of \$55,000.00. Is that the way the books were as of December 31, 1941?

A. That is. That is covered in that Cash Special Account of \$55,000.00.

Q. Now, Mr. Whittaker, was the matter of the organization of this corporation discussed with you by Mr. Carpenter at any time prior to its organization? A. No.

Q. Did you have any discussion with Mr. Carpenter after he came to you for the purpose of having you prepare them a set of books relating to the manner in which the advances made to this corporation would be handled?

A. No, that was not taken up with us.

Q. He didn't tell you that part of the advances were to be treated as loans?

A. Not to my recollection.

Mr. Maiden: I believe that is all, if the Court please.

The Court: Cross-examine.

Cross Examination

By Mr. Webster:

Q. Mr. Whittaker, you have testified that you say the minute book of Wilshire and Western on

(Testimony of Benjamin H. Whittaker.)

October 23, 1941. Did [114] you see it after that date?

A. No. After I had gotten the data from it, I sent it back to Mr. Odell across the street.

Q. Did you ever see any minutes which were later included in the minute book?

A. No, I did not.

Q. Did you ever see any of the stock certificates which were issued by the corporation?

A. No.

Q. Did you ever see any of the notes which were issued by the corporation? A. No.

Q. Mr. Whittaker, in the minutes of the corporation dated July 14, 1941, there is a statement that a portion of the money desired by the corporation would be borrowed. Do you recollect seeing that statement? A. I do not.

Q. You have testified that when you set up the books of account of the corporation you included a notes payable account, is that correct?

A. Yes, of course.

Mr. Webster: Mr. Maiden, will you stipulate I have here the ledger, the general ledger, of Wilshire and Western Sandwiches, Inc.?

Mr. Maiden: So stipulated. [115]

By Mr. Webster:

Q. Mr. Whittaker, I ask you to find for me, if you can, the account titled "Notes Payable."

A. I can't find any accounts in there of any sort or description. I gave them a list of the accounts to be set up, and if they didn't set them

(Testimony of Benjamin H. Whittaker.)

up, it is not my fault. Where it should be, I can point out to you. It should have been in between this point and that point (indicating).

Mr. Maiden: What pages did you refer to, that it should be in between one point and another point?

The Witness: It is not numbered. They did not follow out my numbering.

By Mr. Webster:

Q. In any case, it would have been in the liability section?

A. It should have been in the liability section. It should have been, it was provided for.

Q. After you gave instructions with respect to the opening of the books of account, did you see the books again?

A. I probably saw them in January when they had that trial balance taken off.

Q. Did you take the trial balance?

A. No; my assistant did.

Q. An employee of yours?

A. He happened to be my son. [116]

Q. No relation, in any case, to Wilshire and Western Sandwiches? A. I beg pardon?

Q. He had no affiliation with Wilshire and Western Sandwiches, Inc.?

A. Scarcely, if he was working for me.

Q. Mr. Whittaker, have you in your possession a copy of the information which you submitted to the bookkeeper at Wilshire and Western at the time they set their books up?

(Testimony of Benjamin H. Whittaker.)

A. Why, sure. They had this index and this information, an opening journal entry. These are just the footnotes from which this was dictated (indicating).

Q. Mr. Whittaker, you are showing me now your carbon copy of that portion of the general ledger which appears under the tab, "Journal," and appearing on pages 1 and 2 of that journal.

A. That was typed in my office.

Q. That was typed in your office?

A. That was typed in my office.

Q. And this was approximately at what time, what date?

A. It would have been some time shortly after October 23rd.

Mr. Maiden: 1941?

The Witness: 1941. I might add it is my general practice, in a case of that kind, to provide that opening [117] journal typed in connection with the layout.

By Mr. Webster:

Q. Mr. Whittaker, I point to Account No. 1032, entitled "Stock Subscriptions Receivable," contained under the tab "Assets" in the general ledger of Wilshire and Western. I will ask you whether you have ever seen this page before (indicating).

A. No. The heading seems to have been written in at my office.

Q. You say the heading was written at your office? A. Yes.

Q. Under the column "Date" appears "Decem-

(Testimony of Benjamin H. Whittaker.)

ber 31, 1941" for the first entry, and the posting reference to "J-3" and "ACF \$55,000.00." Turning to J-3, I ask whether you have ever seen the contents of that entry.

A. I have never seen that page before.

Q. Is the handwriting familiar?

A. I don't know whose handwriting it is. It is not from my office; we type everything.

Q. Did you ever give any instructions to anyone at Wilshire and Western with respect to the amount of stock either subscribed for or unsubscribed for?

A. The only instruction that I ever gave to anybody there was that contained in that opening journal entry, which you have typed in the books, the journal that you just showed [118] me.

Q. Mr. Whittaker, in the event that you had seen or had been shown a copy of the notes and the stock certificates prior to December 31, 1941, would you have made any entry on the books?

A. I would not have made any entry on the books of any sort or description.

Q. Would you have given anybody an instruction to make an entry on the books recording the existence of the notes and stock?

A. Yes, I think I would.

Q. Mr. Whittaker, what source did you use to prepare the 1941 tax return?

A. My trial balance taken right from the books.

Q. In the event that the books were incorrect—

A. I was not making an audit. I was preparing a tax return.

(Testimony of Benjamin H. Whittaker.)

Mr. Webster: That is all, your Honor.

The Court: Anything further from this witness?

Mr. Webster: Just a minute.

By Mr. Webster:

Q. Mr. Whittaker, in the event the books were incorporated, would your tax return have been incorrect?

A. It depends when the entries on the books were made. The entries that were on the books when I took the trial [119] balance and had my son work on the trial balance were the ones on which the tax return is made.

Q. But if, in fact, the books were incorrect—

A. You mean out of balance? What do you mean by “incorrect”?

Q. If the books did not accurately reflect the financial position or stock structure of the corporation, then the tax return would likewise not reflect the actual financial position or actual stock structure of the corporation?

A. I don't think that follows at all.

Mr. Webster: That is all, your Honor.

Redirect Examination

By Mr. Maiden:

Q. Mr. Whittaker, when you prepared the 1941 return did you turn it over to Mr. Carpenter?

A. I don't recall whether I did that or whether I sent it up to his office for him. I think my general practice at that time was to send all of them up to Mr. Carpenter's office.

(Testimony of Benjamin H. Whittaker.)

Q. This return shows it was signed by Harry B. Carpenter and H. B. Carpenter, Jr.

A. Yes.

Q. Did either of those officers object to this return as prepared by you?

A. No. I think about what happened was this: that I took the returns up there and I said, "You sign here," and [120] they signed there and put the seal on, and I took it away and signed it myself, and mailed it up to the Division.

Q. You don't know whether they read the return or not?

A. I don't think so. Not very many, none of my clients ever read their returns. The only thing they want to know is, "How much tax do I have to pay?"

Mr. Maiden: No further questions.

Mr. Webster: No further questions.

(Witness excused.)

The Court: We will be recessed until 10:00 o'clock tomorrow morning. Let the record be definite that this witness is excused from further attendance. Is that right?

Mr. Webster: Yes, that is right.

Mr. Maiden: That is right.

(Whereupon, at 5:00 o'clock p.m., an adjournment was taken until 10:00 o'clock a.m., Thursday, December 4, 1947.) [121]

Los Angeles, Dec. 4, 1947

PROCEEDINGS

The Court: Proceed.

The Clerk: The witness taking the stand is Mr. Harry B. Carpenter, who has been sworn.

Whereupon,

HARRY B. CARPENTER,

called as a witness for and on behalf of the Petitioner, having been previously duly sworn, resumed the stand and testified further as follows:

Direct Examination (Continued)

By Mr. Webster:

Q. Mr. Carpenter, you testified yesterday that you had been in the restaurant business for approximately 40 years. A. Correct.

Q. How much of that time in this area?

A. Since 1916.

Q. Southern California? A. That is right.

Q. What type of restaurants did you operate?

A. I formerly operated small lunch counters, seating 12 to 25, until 1930, when I opened my first drive-in, February of 1930.

Q. Since that date what type of restaurants have you operated?

A. After disposing of my lunch counters in 1930, the [125] latter part of '30, I have operated nothing but drive-ins.

Q. Do you operate these drive-ins completely?

A. No.

(Testimony of Harry B. Carpenter.)

Q. That is, by yourself? A. No.

Q. You share the ownership with others?

A. That is right.

Q. At the present time approximately how many drive-ins do you have an interest in?

A. Eight to ten.

Q. These drive-ins are located at different locations? A. Yes.

Q. Do you have the same or a different business unit operating those drive-ins, each of them?

A. They are all separate.

Q. All separate business units?

A. All operated separate. The ones under my supervision have one joint office.

Q. But the corporation or the business unit which owns those drive-ins is different for each drive-in? A. That is correct.

Q. Are those business units partnerships or corporations?

A. Two partnerships and two corporations.

Q. Well, now, you have— [126]

A. I am speaking of the ones I supervise.

Q. With respect to the remaining ones in which you have an interest—

A. They are all corporations.

Q. When did you first enter into the corporate form of doing business?

A. To the best of my recollection, 1938.

Q. Prior to that time you did business in what form? A. Partnership.

Q. Subsequent to that date as a corporation?

(Testimony of Harry B. Carpenter.)

A. Both, both corporation—

Q. Permit me to clarify that question. With respect to new ventures started after 1938—

A. All corporations.

Q. Is there any reason for the fact that subsequent to 1938 any new ventures were in corporate form?

A. Yes. Prior to '38 I would take a lease on a corner and in every instance there was a kick-off clause.

Q. What do you mean by “kick-off” clause?

A. Both the landlord or myself had the privilege of giving 60 to 90 days' notice in canceling the lease. It was restricted on the landlord's part to sale or long-term lease of his property. I had the privilege, for any reason whatsoever, of giving 60 to 90 days' notice, as the case might be, in folding up and moving off. [127]

Q. By the way, Mr. Carpenter, when you speak of you, yourself, having that privilege, you are speaking with respect to the business organization in which you had an interest?

A. That is right.

Q. You say you had this kick-off clause prior to 1938?

A. That is right.

Q. Did anything occur which prevented you from getting that clause after that date?

A. It became harder and harder to get a good corner, as the valuation of the property went up, without signing a direct lease.

Q. How long term of lease would customarily

(Testimony of Harry B. Carpenter.)

be required? A. Ten to fifteen years.

Q. Did this fact you would have to sign a long-term lease, without a privilege of cancellation, have any effect upon your decision to go into a particular location as a corporation?

The Court: Counsel, I call your attention to the fact the witness has not stated he wouldn't have thereafter the privilege of cancellation. That is a kind of inference. It has not been stated. I couldn't consider this evidence.

By Mr. Webster:

Q. Mr. Carpenter, subsequent to 1938 did you ever enter [128] into any leases? Did you, or any business unit in which you had an interest, ever enter into any leases which did have the right of cancellation about which you previously spoke?

A. After 1938?

Q. Yes. A. No.

Q. They were all long-term leases?

A. That is right.

Q. Did this fact have any effect upon your decision to go into new ventures only as a corporation after 1938?

A. Will you please state the question again?

The Court: Read the question, please.

(The question was read.)

The Witness: Well, as I stated previously, I refused at any time to sign a lease that held me for any long length of time on a corner that—something that might break me if the place failed. I wouldn't take the personal responsibility.

(Testimony of Harry B. Carpenter.)

By Mr. Webster:

Q. Mr. Carpenter, do you know Mr. M. A. McDonnell? A. Quite well.

Q. How long have you known him?

A. Forty years.

Q. Where did your acquaintance first occur?

A. Kansas City, Missouri. At that time Mr. McDonnell had a place, a restaurant, on one street, and I had one on the other, around the corner, and our kitchens were next door to each other. We used to meet in the alley and talk the restaurant business over, 40 years ago.

Q. Do you know when Mr. McDonnell came to California?

A. He came in 1916, in the fall; I came in the spring.

Q. Have you been in contact with each other after you came to California? A. Yes.

Q. Are you familiar with his manner of doing business? A. I am.

Q. Do you know whether he met the same type of situation which you have previously described with respect to this cancellation clause?

A. I personally know that he has never signed a lease since coming to California that he couldn't cancel upon certain days' notice, certain length of time.

Q. By "personally" you mean what?

A. We discussed the matter many, many times, and it was upon his advice that I have always operated on the kick-off clause, or a corporation.

(Testimony of Harry B. Carpenter.)

Q. Mr. Carpenter, in view of your long experience in the restaurant business, would you state to the Court your opinion as to the relative safety or relative hazards [130] associated with the restaurant business?

A. Well, I have belonged to the National Restaurant Association since its organization about 1917. I have attended many of the conventions, and it has been discussed by the leading restaurant men in the United States as considering it the most hazardous line of business there is.

Q. Have you ever had any interest in the past in restaurants which have failed?

A. Yes, I have.

Q. Mr. Carpenter, you have stated that you have had a separate business unit since 1938, and that business unit was a corporation for each location.

A. That is right.

Q. Can you state why that was so?

A. Why the separate corporations were formed?

Q. For each location.

A. That was to prevent, in case of failure, of one large investment, of the tearing down of all the places and tearing them all down.

Q. Turning now to the particular corporation with which we are concerned, Wilshire and Western Sandwiches, Inc., do you recollect when this deal was first discussed?

A. Very early in 1941.

Q. Mr. Carpenter, you were in court yesterday, were you not, when testimony was received from

(Testimony of Harry B. Carpenter.)

Mr. Simon to the [131] effect that the original thought was to open a combination drive-in and bar on the southwest corner of Wilshire and Western Avenue, and that this deal fell through and that Mr. Simon had negotiated a lease on the northwest corner of Wilshire and Western, which lease was assigned to Wilshire and Western Sandwiches, Inc. Are those facts correct?

A. Those are facts as he stated yesterday. I had been located on this other property for a good number of years. I approached the landlord and asked him if he would advance a portion of the money if we formed a corporation in connection with Mr. McDonnell, Mr. Simon, and Mr. Lyman, and put in a larger place occupying the entire block.

I occupied half of it at the time. He was very receptive to the idea and we entered into negotiations for lease. I went East to get a very well known restaurant man who was working as the manager of a large restaurant, and attempted to persuade him to come out and take charge of this place and run it for me.

Q. Pardon me, Mr. Carpenter. Do you know approximately when it was you made this trip?

A. That was in 1940, in the fall of 1940. I also attended the National Restaurant Convention on the same trip. He and his wife were loath to leave Chicago, so I came back and told Mr. Simon, Mr. McDonnell, that as far as I was concerned the deal was off. It was too large a restaurant for [132]

(Testimony of Harry B. Carpenter.)

me to attempt to run, in connection with my other places, and I preferred to pass it up.

In the meantime Mr. Simon was negotiating for a smaller unit, for just a straight drive-in, on the northwest corner of Wilshire and Western.

Q. In whose name was the proposed large place on the southwest corner to be in, that is, under what name was that place proposed to be operated?

A. Carpenter.

Q. At the time that Mr. Simon was negotiating this lease on the northwest corner, under what name was the proposed location to be operated?

A. Those negotiations were started while I was East. I don't know. I think that he intended to operate that in addition to the one that I might put in on the south corner. But the lease was drawn up and it was drawn up in Mr. Simon's name, with the understanding that he could transfer it to a corporation and it wouldn't be under any obligation to pay the rent after the corporation received the lease. He assigned it to the corporation.

Q. When did you first speak of forming Wilshire and Western Sandwiches, Inc.?

A. That was in connection with the other place, originally. I insisted, by the way, after I came back and we all agreed to go ahead and form the corporation and operate the [133] smaller unit, that as long as I had been on this corner for approximately 11 years, that I still be allowed to operate under my trade name. I felt it was a very well

(Testimony of Harry B. Carpenter.)

known one and we had a good reputation in the neighborhood.

Q. Was there any understanding about that time as to who would be in active supervision over that location that the taxpayer now occupies?

A. After making this assertion, it was agreed by all I could operate the place.

Q. Now, there was no drive-in on the property in early 1941, was there?

A. On the present property?

Q. On the present property. A. No.

Q. Was there any understanding as to who would supervise the construction of that drive-in?

A. Yes, the operator was to do that, myself.

Q. That is, you? A. Yes.

Q. Do you hold any office in Wilshire and Western Sandwiches? A. Yes.

Q. What office? A. President.

Q. Mr. Carpenter, do you recall any discussions with [134] respect to the capital structure of Wilshire and Western Sandwiches in early 1941?

A. Yes.

Q. What was the nature of those discussions?

A. Well, the other boys seemed to think that we could erect and equip the drive-in for a maximum of \$30,000.00. I told them that I had opened between 40 and 50 restaurants and drive-ins, and that I had always found that the cost exceeded the estimate. I felt that we should plan on at least \$50,000.00.

Q. Was there any discussion with respect to the

(Testimony of Harry B. Carpenter.)

amount of money which was to be put in by—
Strike that question.

With whom were these discussions?

A. Mr. McDonnell, Mr. Simon, and Mr. Lyman and myself.

Q. Was there any discussion at this time, which was early 1941, with respect to the amount of money which would be paid in by the four of you?

A. Yes. We agreed to pay in the \$30,000.00, but we would split it up on a fifty-fifty basis in regard to what we called an investment, always we considered capital stock. We always took notes for what we called a loan. We had done this previously.

Q. You actually had a discussion on that subject at that time? A. Yes. [135]

Q. Did the others agree on this method of—

A. Yes.

Q. Mr. Carpenter, the corporation is authorized, under its articles of incorporation, to issue a total of \$75,000.00 worth of stock, 7,500 shares at \$10 per share at par? A. I think that is correct.

Q. Can you explain how that amount was arrived at?

A. Yes. I went up to my attorney's office.

Q. Pardon me. Your attorney?

A. Mr. Robert Odell—and asked him to draw corporate papers and form a corporation called Wilshire and Western Sandwiches, Inc.

I don't remember his exact words, but they virtually were to the effect, "How much do you want to incorporate for?" I named some sum, approxi-

(Testimony of Harry B. Carpenter.)

mately what I thought the cost might be—I don't remember — somewhere around \$35,000.00 or \$40,000.00.

He said, "It doesn't cost any more to form a corporation with capital stock of \$75,000.00, because I am going to form one that has broad powers. You can buy and sell real estate. You don't know what might come up in the future, what you might want to do. It won't do any harm."

I said, "You draw it up."

Q. Mr. Carpenter, what was your own personal feeling with respect to these discussions as to a part-stock, part-loan [136] basis?

A. What was my personal opinion?

Q. Yes. Were you in favor of it or against it?

A. Oh, yes, I was very much in favor of it.

Q. Can you state why you were in favor of it?

A. Well, we knew that if we took the whole thing in stock, the ever-present possibility of a failure entered into the picture, and we would lose probably the entire investment because you can't ever realize 100 per cent on a failure. So we thought that if we took 50 per cent in stock and 50 per cent in notes, as we had done in the past, that we would at least come in with the creditors in case of failure and realize part of our investment.

Q. Mr. Carpenter, it has been stipulated, that is, counsel for the Government and counsel for the Petitioner have agreed, that you took part in other corporations in which there was a part-stock,

(Testimony of Harry B. Carpenter.)

part-note setup. These corporations are as follows: F. & L. B. Corporation, which commenced business in October of 1941; Carsim, Inc., which commenced business in June of 1939; Simon's Florat, Inc., which commenced business in November of 1941; Simon's Five Points, Inc., which commenced business in November of 1941; and Sunset Sandwiches, Inc., which commenced business in January of 1941.

With respect to those corporations which I have just [137] named, did you receive stock certificates from those corporations? A. I did.

Q. Did you receive notes from those corporations? A. I did.

Q. Did you consider yourself both a stockholder and a lender to those corporations?

A. Yes, sir.

Q. Can you state why you entered into a part-loan, part-stock arrangement with respect to those other corporations?

A. Well, in each instance I was a minority stockholder and I had no say as to what dividends might be paid. But as a noteholder I could demand repayment of the note on the day it matured or soon thereafter.

Q. Were any of the considerations which you thought of in the Wilshire and Western deal present in these other deals?

A. They were all very similar.

Q. Had you discussed these points with the other gentlemen whom you entered into the trans-

(Testimony of Harry B. Carpenter.)

actions with? A. Many, many times.

Q. Were you in agreement with them?

A. Yes.

Q. I would like to turn for a moment to the subject of your estimates as to the cost of erecting the drive-in at Wilshire and Western. When the deal was first discussed, [138] what is your recollection of your estimate at that time?

A. My estimate was that it would be closer to \$35,000 than \$30,000.

Q. Upon what basis did you make this estimate?

A. Because I had just supervised the erection and opening and operation of Sunset Sandwiches, which, if I remember correctly, we opened in January of this same year, 1941. That place cost \$34,000, by the way.

Q. Pardon me?

A. That place finished up with a total of \$34,000, I think, even to the dollar.

Q. Had you formed an estimate as to the relative cost of the building and of the equipment?

A. It was the usual procedure to estimate 50 per cent, and ordinarily it didn't vary very far from that.

Q. By 50 per cent you mean—

A. Half building and half equipment and fixtures.

Q. It has been stipulated, Mr. Carpenter, that in June of 1941 you received four bids from four different contractors to erect the building, and that

(Testimony of Harry B. Carpenter.)

one of these bids was from Frank A. Woodyard in the amount of \$18,222. A. That is correct.

Q. Did this bid fit in with your idea of what the approximate cost would be?

A. It wasn't very far off. [139]

Q. It has also been stipulated that in July, on July 10th of 1941, a construction contract was entered into between the corporation and Mr. Woodyard for \$22,651, or approximately \$4,400 more than the original bid. Did this have any effect upon your estimate at that time, of what the cost of the drive-in would be?

A. I felt it would increase it the amount of the increase in the bid, but I didn't think that it would cause the fixtures to run any higher. There were some certain changes the architect made in the building plans. I think one of them was extending the size of the canopy.

Q. As time went on, Mr. Carpenter, did your estimate prove to be accurate or inaccurate?

A. It proved to be inaccurate.

Q. When did you commence discovering this inaccuracy?

A. The first intimation I had that we might run into considerable more money was when the City Building Department made us—increased the strength of the canopy I just spoke about, because of the fact we had enlarged it, made it cover a larger area of the car; and several other changes from the Building Department.

Q. At approximately what date did that occur?

(Testimony of Harry B. Carpenter.)

A. Oh, it was either in August or early September.

Q. It has been stipulated that on July 17th of 1941, a permit was granted from the California Corporation [140] Commissioner to issue shares of stock of Wilshire and Western Sandwiches. Do you know whether any shares of Wilshire and Western Sandwiches were ever issued?

A. Yes.

Q. When were they issued?

A. They were issued sometime after the place opened in November.

Q. Can you account for the delay between the date of the permit and the date when the stock certificates were issued?

A. Yes, because we couldn't determine the amount to be issued in stock or the amount to be issued in notes until we had a better idea of the complete cost of the opening of the unit.

Q. Mr. Carpenter, it has been stipulated that in May and June of 1941 you, Mr. Simon, Mr. Lyman, and Mr. McDonnell contributed a total of \$10,000 to the corporation, that is, paid in. Also, it has been stipulated that in August and September these same four individuals contributed \$15,000 or paid in \$15,000, and that in October you, Mr. Simon, and Mr. Lyman paid in \$10,000, and that in November the four of you paid in \$20,000. Was anyone responsible for the fact that these payments were spread out the way they were?

A. Yes, I was. [141]

(Testimony of Harry B. Carpenter.)

Q. Can you describe to the Court the circumstances surrounding these payments?

A. Well, the bank account was in my name and I was supervising the building of the building and the ordering of the fixtures. I paid all the bills. As the bank account began to get low, I would call for more money and put in my share along with the rest of them.

Q. You say you would call for money. Physically, how would you go about doing that?

A. I would call them up and in some instances I probably went down; in fact, I know I made many trips to Mr. Simon's office.

Q. When did you arrive at the conclusion that you had received a sufficient amount of money to cover the cost?

A. After the place opened up, shortly after the 5th of November.

Q. By the way, Mr. Carpenter, you stated that the bank account was in your name. Could you tell why it was in your name?

A. Somebody had to—always the man that was to operate the unit had the bank account in his name. I say it was in my name; it was in the name of Wilshire and Western, and I was authorized to sign the checks.

Q. I see. You say that shortly after the drive-in opened in November you felt that you had received a sufficient [142] amount of money?

A. Well, I called the boys up a week, such a matter, after I opened up and asked them to come

(Testimony of Harry B. Carpenter.)

out and see the place. They hadn't been near it. So they all came out, and while they were there I discussed the finances. I told them that we had—we were going to spend a lot more money than we had ever anticipated spending, so I thought we should decide on the amount of stock to be issued and the amount in notes, and we discussed it informally at the counter of the drive-in.

The amount of money I had spent didn't seem to disturb them, so I got in touch with Mr. Odell and told him we had arranged to have a meeting the following day—I don't remember the exact date—in Mr. Simon's office, and told him exactly what we had agreed on. He typed out the minutes and accompanied me the following day to Mr. Simon's office where we had the meeting.

Q. You say you agreed as to the amount of money you required. Do you know how much money was paid in? A. At that time?

Q. At that time.

A. I don't remember exactly how much; I know Mr. McDonnell was a little lax with his last payment. I had to phone his office several times trying to get in touch with him and chase him down. [143]

Q. Counting that last payment as committed to but actually not paid, how much money by the time you had held your meeting—

A. \$55,000.

Q. \$55,000? A. That is right.

Q. And at the time of the informal meeting at the drive-in, about which you have testified—

(Testimony of Harry B. Carpenter.)

A. Yes.

Q. —was there an understanding as to the—

Mr. Maiden: Your Honor, I object to his leading the witness. Let the witness tell what occurred at these conferences.

The Court: Don't lead your witness. You have heard what I said about leading testimony. I mean it.

Eventually I have to evaluate the evidence, coming to my conclusion; regardless of whether there is an objection on account of its being leading, the fact you lead the witness logically makes the answer partly yours, rather than the witness'. I discount it to that extent. Now, for your own benefit—

The Witness: I know exactly—

The Court: I am not talking to you, Mr. Witness.

For your own good, don't lead the witness. That applies just as equally to one side as the other.

By Mr. Webster:

Q. Mr. Carpenter, I show you Petitioner's Exhibit 12, which is a written consent and waiver notice of a directors' meeting, and attached to that are the minutes of a meeting of the board of directors of Wilshire and Western Sandwiches, Inc.

A. What date?

Q. Consisting of five pages. The date is November 13, 1941. I ask you whether the signature on the written consent and waiver of notice, appearing on the second line, is yours? A. Yes.

(Testimony of Harry B. Carpenter.)

Q. Turning to the last page of the minutes, over the line for signature, calling for the signature of the president, I ask whose signature that is.

A. That is mine.

Q. Have you even seen these minutes?

A. Yes, they look very familiar.

Q. When did you see them?

A. I saw them at the meeting when Mr. Odell brought them up to Mr. Simon's office.

Q. Did you sign them at that meeting?

A. Yes.

Q. Did you read them over at that meeting?

A. Mr. Odell read them to all of us. Mr. Odell being a man who very—oh, I don't know how to explain it—he [145] insisted that everything be regular, that the meeting be called to order in the proper way and that the vote be taken on the various matters of the minutes, or what not. I don't think there was ever a meeting held that amounted to anything—we might meet informally and discuss something—there was never a meeting held where there were any minutes drawn up in either this or any other corporation that Mr. Odell had anything to do with that he didn't insist on being present.

Q. Were you present at the time the other individuals signed those minutes?

A. Yes.

Q. You stated that Mr. Odell read the minutes to you?

A. That is right.

Q. Was there any discussion following the reading of those minutes?

(Testimony of Harry B. Carpenter.)

A. I can't recall any now, any more than they were approved and signed and agreed to. I might add, if I could, that when the informal meeting took place at Wilshire and Western at the counter, that I told them I was sure it would go as high as \$55,000 and might run over a thousand or two, but I felt we were going to have a successful operation and I could pay out the balance out of the profits as they came in, and we wouldn't have to advance any more money.

Q. Did Mr. Odell call for a vote of the people who were present? [146] A. Yes.

Q. Did he call for a vote on each resolution?

A. Yes.

Q. Was this customary? A. Yes.

Q. It was Mr. Odell's practice?

A. With Mr. Odell, yes.

Q. How long have you had Mr. Odell as an attorney?

A. Thirty years, or thirty-one; I met him very shortly after I came to California.

Q. It has been testified that by the end of November of 1941 a total of \$55,000 had been paid in.

A. That is correct.

Q. Did this turn out to be sufficient?

A. No.

Q. Then you describe what circumstances later took place.

A. Along towards the first of the year, when the miscellaneous bills came in, some of them I had forgotten about and others were much larger than

(Testimony of Harry B. Carpenter.)

I had anticipated, and I had to call the boys up and apologize to them and say, "Fellows, we are going to have to have another \$10,000. I would like to borrow that without issuing any notes, and pay it back probably before the end of the year."

One of the reasons for the increase was the fact that [147] I had been kicked off the corner across the street, or notified on the 60 or 90 days' notice, whichever it was, and I had to move from over there on the first day of November. As a matter of fact, I was supposed to have my building cleared off by the 1st of November. They gave me an extra week to get the building off, so I operated the business working day and night, trying to get Wilshire and Western open by the 1st of November. I missed it five days. I continued to operate the old place until we operated the new, and then got busy and tore down and left the lot in first-class condition at the old location.

Q. Did the other three whom you contacted send in any money? A. Yes.

Q. What were the amounts?

A. I put in thirty-three hundred thirty-three dollars and some cents. McDonnell did likewise, and Simon and Lyman between the two of them put in an equal amount, making the \$10,000.

Q. Do you recall approximately when that money was paid in?

A. It was after the first of the year, probably after the first of February.

Q. Did you issue any notes?

(Testimony of Harry B. Carpenter.)

A. No, not for that \$10,000. [148]

Q. Was any interest paid? A. No.

Q. Do you know whether this \$10,000, of which you speak, was repaid?

A. Yes, it was repaid and it was repaid before the end of the year, if I remember correctly.

Q. Mr. Carpenter, I show you Check No. 793, Check No. 794, and Check No. 795, all bearing the imprint in the lower right-hand corner, "Wilshire and Western Sandwiches, Inc." They are made out to Mike Lyman, M. A. McDonnell, and H. B. Carpenter, and they bear in the upper right-hand corner a description "Note Account." The date of all three of them is September 7, 1942. I ask you if you recollect these checks. A. Yes.

Q. Is that your signature (indicating)?

A. In every instance.

Q. What was your understanding with respect to these checks?

A. That they were the repayment of that \$10,000 that I called for and received early in '42.

Q. Do you recall making out a similar check for Mr. Simon? A. I do.

Mr. Webster: I offer these as Petitioner's exhibits [149] next in order.

The Clerk: One exhibit or three separate exhibits? Mr. Webster: One exhibit.

The Clerk: Exhibit 16 has been offered, your Honor.

The Court: Three checks identified by the witness will be admitted in evidence as Exhibit 16 for the Petitioner.

(Testimony of Harry B. Carpenter.)

(The checks above-referred to were received in evidence and marked Petitioner's Exhibit No. 16.)

Mr. Shearer: If your Honor please, Petitioner's 15 is a similar check. It might avoid confusion if they were all added to Petitioner's 15, if that were possible.

The Court: I see no reason to do that.

Mr. Shearer: All right.

The Clerk: The checks have been marked No. 16 in evidence.

By Mr. Webster:

Q. Mr. Carpenter, what was your intent with respect to the \$3,333.33 which was paid in by you in February of 1942?

A. The intent? The intent was to loan the money to the corporation so the corporation could pay the unpaid bills.

Q. It has been stipulated that outside of this last amount which I have just spoken of, that you advanced a total of \$18,333.33, and it has also been stipulated that these advances took place between June and November of 1941. Can you state what your intent was at the time of each advance? [150]

A. My intent at the time of each advance was that the total amount should go into the treasury of the corporation and that in due time I would be issued stock and a note for approximately 50 per cent of each payment.

Q. Mr. Carpenter, I show you a rectangular black book and ask you if you can identify it.

(Testimony of Harry B. Carpenter.)

A. Yes, that is the stock book of Wilshire and Western Sandwiches, Inc.

Q. Have you ever seen it before?

A. Many times.

Q. Where did you see it?

A. In Mr. Odell's office.

Q. Did you ever place your signature in the book or on any pages of the book?

A. Yes, I signed a receipt for any stock and signed each stock certificate before it was issued.

Q. Mr. Carpenter, I call your attention to a stub bearing the imprint "Certificate No. 3," and attached to this stub is a certificate which is numbered "No. 3." Both the stub and the certificate indicate they were issued to William H. Simon.

A. That is correct.

Q. Do you recall signing the certificate?

A. Yes.

Q. Can you explain why this certificate is in this [151] book?

A. Yes. Simon told me that he wanted to give Joe Lerdemer, his general manager, an interest in his investment of this corporation. In authorizing Mr. Odell to issue these shares of stock I forgot it.

Q. When did Mr. Simon tell you about wanting to make a gift?

A. It was along during 1941; I don't remember.

Q. Can you place it with respect to the fall or the summer or the spring?

A. I would say either late spring or early summer. And these shares were issued and mailed or

(Testimony of Harry B. Carpenter.)

delivered, I guess—no. I don't remember whether I took them up or Mr. Odell took them up. Anyway, he asked me to have the shares re-issued, giving Mr. Lerdemer a percentage. I think it was ten percent of both Mr. Simon's and Mr. Lyman's investment in this corporation, of their stock.

Q. Had Mr. Lyman spoken to you about making—

A. No, Mr. Lyman talked very little in regard to the affair. After this came up they both instructed me to have Mr. Odell re-issue these shares decreasing their holdings ten percent, in each instance, and giving the ten percent to Joe Lerdemer.

Mr. Webster: I offer this stock book in evidence as Petitioner's exhibit next in order. [152]

The Court: The last number was sixteen. The stock book is admitted in evidence as Petitioner's Exhibit 17.

(The stock book above-referred to was received in evidence and marked Petitioner's Exhibit No. 17.)

By Mr. Webster:

Q. Mr. Carpenter, the stock book which you were just looking at shows that one thousand shares were issued to you. Did you receive those shares?

A. Yes.

Q. When did you receive them?

A. Oh, a short time after the—after the meeting we held in Simon's office, possibly two weeks, possibly a month; I don't remember.

Q. Mr. Carpenter, I show you a letter on the

(Testimony of Harry B. Carpenter.)
stationery of Tanner, Odell & Taft, dated December 5, 1941, and addressed to you, and ask whether you have ever seen this letter before?

A. Yes, the note and the stock came along with this letter to my office.

Q. Are you familiar with Robert Odell's signature? A. Yes, indeed.

Q. Is this his signature (indicating)?

A. It is. [153]

Q. You say this was the letter which transmitted your stock certificate and note?

A. And note; they came together.

Q. Can you recall when you received this letter?

A. Well, it is dated December 5th. I certainly received it very shortly thereafter.

Q. There was nothing unusual about the date of the letter with respect to the date of receipt of it?

A. No.

Mr. Webster: Your Honor, I offer this letter in evidence as Petitioner's exhibit next in order.

The Court: Is there any objection?

Mr. Maiden: No objection, your Honor.

The Court: The letter as identified by the witness is received in evidence as Petitioner's Exhibit No. 18.

(The letter above-referred to was received in evidence and marked Petitioner's Exhibit No. 18.)

By Mr. Webster:

Q. I show you three documents and ask you to identify them.

(Testimony of Harry B. Carpenter.)

A. These are all notes of the corporation, signed by me.

Q. One of them is made out to M. A. McDonnell in the amount of \$8,333.33. This is your signature (indicating)?

A. Yes, it is.

Q. Another is made out to Mike Lyman in the amount of [154] \$4,166.66, and is this your signature on it (indicating)?

A. That is.

Q. And a third is made out to Harry B. Carpenter in the amount of \$8,333.34. Is this your signature on it (indicating)?

A. It is.

Q. These notes are dated November 13, 1941. Do you recollect when you signed these notes?

A. Well, I would say I signed them on that date, November 13th, but I am not absolutely positive now. That would be awfully hard to say. I don't remember where I signed them, either, whether it was at this meeting or over at Mr. Odell's office.

Q. If it wasn't on November 13th, was it—you would say it was close to that date?

A. Yes.

The Court: You are leading your witness. The witness said he didn't know. Let it go at that. Don't try to get him to say something different.

Mr. Webster: I offer these three notes in evidence.

The Court: Offer them one at a time.

The Clerk: No. 19.

The Court: Petitioner's Exhibit 19. What is Exhibit 19, the size of the note?

(Testimony of Harry B. Carpenter.)

The Clerk: \$8,333.34, dated November 13, 1941.

The Court: Admitted in evidence.

(The note above-referred to was received in evidence and marked Petitioner's Exhibit No. 19.)

The Clerk: Note dated November 13, 1941, in the amount of \$4,166.16, is No. 20.

The Court: Admitted in evidence.

(The note above-referred to was received in evidence and marked Petitioner's Exhibit No. 20.)

The Clerk: No. 21, dated November 13, 1941, in the amount of \$8,333.33.

The Court: Admitted in evidence.

(The note above-referred to was received in evidence and marked Petitioner's Exhibit No. 21.)

The Witness: I might add to that, that the reason I don't think they were signed or even made out at this meeting was because my son's signature is on there with me, and he wasn't present at the meeting.

By Mr. Webster:

Q. Mr. Carpenter, what was your intent with respect to the \$8,333.34, represented by the note?

A. I was to loan it to Wilshire and Western Sandwiches, Inc., and receive interest on it, and to be paid in full if we ever got enough money to pay it with, along with the others.

Q. Have you ever thought of going to a bank to borrow the money? [156]

(Testimony of Harry B. Carpenter.)

A. Yes. We discussed going to a bank to borrow money. And we all agreed that we would rather receive the interest on the money at a pretty good rate of interest than to pass it along.

Q. Mr. Carpenter, it has been stipulated that on April 21, 1943, a check was issued to you in the amount of \$3,333.34, with an explanation in the voucher portion of the check which read, "Payment on note." Do you recall receiving this check?

A. Yes.

Q. What was your understanding?

A. That that was a payment on the note.

Q. It has been stipulated that on May 23, 1944, a check was issued by the corporation to you in the amount of \$3,333.33, and that the explanation in the voucher portion of the check reads, "Note Account." Do you recall receiving this check?

A. Yes.

Q. At about the time of the check?

A. Correct.

Q. And what was your understanding?

A. It was repayment of the note.

Q. On May 23, 1945, it has been stipulated that a check was issued by the corporation in the amount of \$1,666.66, bearing an explanation in the voucher portion of [157] the check, "Balance on note." Do you recall receiving that check?

A. Yes, I do.

Q. What was your understanding at the time of receipt?

A. That the notes had been paid in full.

(Testimony of Harry B. Carpenter.)

Q. Mr. Carpenter, I show you Checks Nos. 2045, 2047, and 2048, bearing the imprint in the lower right-hand corner, "Wilshire and Western Sandwiches, Inc." Two of them have an explanation in the voucher portion, "Interest to November 30, inclusive." The third one has an explanation, "Interest to November 1, inclusive." Do you recall seeing these checks? A. Yes, I do.

Q. Is that your signature on the checks (indicating)? A. Yes; every one.

Q. Do you recollect what the purpose of these checks was?

A. Yes, it was to pay the interest to the date on the—the day before the date on the check. This is just an error, "November 1"; it should read "30th".

Q. You are speaking about Check No. 2048?

A. That is right.

Mr. Webster: I offer Check No. 2045 in evidence as Petitioner's next in order.

The Court: Admitted in evidence as Petitioner's Exhibit 22. [158]

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 22.)

Mr. Webster: Check No. 2047.

The Clerk: 23.

The Court: Admitted in evidence as Petitioner's Exhibit 23.

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 23.)

(Testimony of Harry B. Carpenter.)

Mr. Webster: Check No. 2048.

The Court: Admitted as No. 24 by the Petitioner.

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 24.)

By Mr. Webster:

Q. Mr. Carpenter, were there any previous payments of interest prior to the payments represented by this check? A. I think not.

Q. Do you happen to know why?

A. I have to say carelessness, I imagine.

Q. Carelessness on whose part, would you say?

A. That is self-evident.

Q. Mr. Carpenter, I show you next Nos. 4134, 4141, and 4146 of the Wilshire and Western Sandwich, Inc., all dated March 23, 1945, and they all have an explanation, "Interest on note to March 24." I ask you if you recall seeing these checks.

A. Yes.

Q. Is that your signature (indicating)?

A. It is.

Q. What was your understanding at the time of making out those checks?

A. This was the interest on the notes to this date; probably in full. I don't remember.

Q. By the way, with respect to this payment, was a check made out to Mr. Simon?

A. Yes.

Q. At this time?

A. I am sure. Let me see them. Well, if there

(Testimony of Harry B. Carpenter.)

wasn't, it was certainly a gross error on the book-keeper's part.

Q. A check is in evidence which was made out to Mr. Simon as of this date. Do you recall having made that out?

A. Well, I don't recall it individually, but I would assume that I did. Anyway, those are my signatures.

Q. They are? A. Yes.

Mr. Webster: We offer Check No. 4134.

The Court: Admitted in evidence as Petitioner's Exhibit No. 25.

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 25.)

Mr. Webster: Check No. 4141. [160]

The Court: Admitted as No. 26 for the Petitioner.

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 26.)

Mr. Webster: Check No. 4146.

The Court: Admitted as Petitioner's Exhibit No. 27.

(The check above-referred to was received in evidence and marked Petitioner's Exhibit No. 27.)

By Mr. Webster:

Q. Mr. Carpenter, did you know anything about—what do you know about the books of account at Wilshire and Western Sandwiches?

(Testimony of Harry B. Carpenter.)

A. I don't know anything.

Q. Who was in charge of the books?

A. At the present time?

Q. Yes.

A. Mr. Tompkins. That might be a little confusing to me. Do you mean the bookkeeper that I employ in my office or the accountant that transfers the accounts in my office onto the set of books of the corporation?

Q. I mean the latter.

A. That is Mr. Tompkins.

Q. Has he always been your accountant?

A. No.

Q. Who was your accountant previously?

A. In the first place it was Colonel Whittaker. The [161] second was Mr. E. J. Aye. When Mr. Aye retired, Mr. Tompkins took the account over personally.

Q. How long was Mr. Whittaker retained by you? A. After the corporation—

Q. Yes. A. I would say—

Q. I mean as to how long it was that Mr. Whittaker was retained by the corporation.

A. I don't think he ever did any work after preparing the income tax for the year '41. He might possibly have worked another month; might have entered one more month's statements.

Q. What was the reason for his leaving?

A. Dissatisfaction; dissatisfied with him.

Q. Pardon me?

A. I was dissatisfied with his services.

(Testimony of Harry B. Carpenter.)

Q. Whom did you then employ?

A. Mr. Aye.

Q. Mr. Carpenter, there has been admitted in evidence Exhibit 8-H, a copy of the 1941 tax return of the corporation. Do you recall signing that return? A. I do.

Q. Did you read it over prior to signing it?

A. No. Mr. Whittaker expressed it correctly, exactly, when he says, "Where do I sign and how much do I pay?" [162]

The Court: We will be recessed at this time for ten minutes.

(Short recess taken.)

By Mr. Webster:

Q. Mr. Carpenter, you have just testified that you signed the 1941 tax return of the corporation, which was Exhibit 8-H. What were the circumstances surrounding your signature or the signing of that return?

A. I think I answered that.

Q. I will withdraw that question.

Do you recollect signing any other tax return with respect to the calendar year 1941?

A. Yes, I think there was an amended return. I know there was one prepared by Mr. Aye.

Q. Do you recollect what the circumstances were surrounding the signing of that return?

A. The only thing that I remember is that we showed that we overpaid our tax in '41, and we asked for a refund; that is all I can remember about it.

(Testimony of Harry B. Carpenter.)

Q. Did Mr. Aye bring that return to your office?

A. Yes.

Q. When?

A. I think very shortly after he took charge of my books.

Q. When was that? [163]

A. That was in April, approximately April of '42.

Q. Of 1942? A. Yes.

Q. Did he leave the return with you?

A. No, he took it with him and left me a copy. And Colonel Whittaker left me a copy of the original when he signed it. But I don't know where they are.

Q. Mr. Carpenter, did you ever enter into any agreement with a creditor of Wilshire and Western Sandwiches under which you subordinated your rights under your note to the rights of any creditor?

A. No, sir, positively not.

Mr. Webster: That is all, your Honor.

The Court: Cross-examine.

Cross Examination

By Mr. Maiden:

Q. Mr. Carpenter, at the time of the organization of this corporation it was the intention of you and your associates to advance to the corporation such money as it needed to build its building and equip it and open it for business, is that correct?

A. That is correct.

Q. You considered that the whole amount of

(Testimony of Harry B. Carpenter.)

the money you advanced was an investment in the business?

A. I considered 50 per cent of it as an investment in [164] stock, and the other 50 per cent as notes, as a debt on the corporation.

Q. Why weren't you willing to invest your share of the total cost necessary for the business to begin operations?

A. Why wasn't I—what was the word you used there?

Q. Why weren't you willing—

A. "Willing"—

Q. —to invest the entire amount of your portion of the total amount of money necessary for the corporation to open its doors for business?

A. Principally because of the hazardous undertaking and the fact that if the business failed I would come in equally with the other creditors on 50 per cent of the money I had put into the organization.

Q. Well, since it was so hazardous, why were you willing to invest any money in the business?

A. I either had to do business or starve to death.

Q. Was it in your mind to become a creditor of this corporation so that if the corporation failed you could come in with the other creditors and keep them out of some of the money that the corporation owed them?

A. I think I stated I would share equally with them.

(Testimony of Harry B. Carpenter.)

Q. Well, in sharing equally with the creditors of your corporation, you would in effect be taking that much money away from the satisfaction of their debts, wouldn't you? [165]

A. I would alter that by saying I wouldn't take near as much away from them as they would take away from me, in the event of failure.

Q. But the debts would have been created upon the good faith and credit of the corporation, of which you and these gentlemen were in control?

A. I think my debt was created the same way.

Q. Wouldn't you consider the necessary debts in the operation of this business a moral obligation on you?

A. I will answer that by saying that I have always paid every debt to date, since I have been in business, and don't owe anybody a dollar.

Q. Isn't it a fact, Mr. Carpenter, that you and these gentlemen conceived this plan or arrangement in order that you could receive a return out of your current earnings of a large portion of your capital without having to pay any tax on it, and at the same time to allow the corporation to make payments to you of interest out of current earnings which would otherwise be dividends, and get a tax benefit from it?

A. Mr. Maiden, you are too fast for me. I can't follow you.

Mr. Maiden: Read the question.

The Court: Read the question.

(The question was read.) [166]

(Testimony of Harry B. Carpenter.)

The Witness: I will answer that as no, and verify it by stating we would have taken the notes and had the same setup if the tax proposition hadn't entered into it. We would have protected ourselves in the same manner.

By Mr. Maiden:

Q. Were you aware of the tax benefit this arrangement would bring to you and the corporation?

A. I was.

Q. Do you mean to tell this Court that did not influence in the least the formation of this arrangement?

A. I said that the same formula would have been carried out if the tax feature hadn't been there.

Q. So that you deny that you were in the least motivated in the formation of this arrangement by tax benefit? A. I do.

Q. You were aware of the fact, weren't you, Mr. Carpenter, that in 1941 the tax rates had begun to increase considerably?

A. I thought the big increase came in the fall of '41; I don't remember.

Q. Being a businessman, you are always conscious and have always been conscious of the important part of federal taxation?

A. That is right.

Q. Now, what difference actually did it make to you, [167] so far as getting your money back—forgetting the tax angle—whether you held this entire amount of money as stock or part of it in notes?

(Testimony of Harry B. Carpenter.)

A. What difference did it make in getting the money back?

Q. Yes.

A. It would have made a great difference had the place not been successful.

Q. How would it have been a great benefit if it hadn't been successful?

A. Well, we started out immediately by depreciating the building and equipment, and as the place went along, even if it had only made a few dollars a month, instead of making more than that, we would have still had accumulated enough money to have paid off the notes where we probably never could have paid any dividends on stock.

Q. How do you know you would have accumulated enough money to have paid off the notes?

A. I don't know it, of course, any more than I knew about any of the businesses I had started; I have had some that failed and some that didn't.

Q. This corporation had to make money before it could set up any reserve for depreciation.

A. It had to make at least that much.

Q. I want to ask you, as a fact, Mr. Carpenter, did [168] this corporation each year set aside a cash reserve for depreciation?

A. It showed on the book; there wasn't a separate bank account made for it.

Q. Was cash actually earmarked and set aside in the bank account for depreciation? You just look at me, Mr. Carpenter.

A. I am answering your questions just as truth-

(Testimony of Harry B. Carpenter.)

fully as I can. I say there was never but one bank account. The books each month showed the depreciation on the fixtures and the building, and I knew at the end of each month where I stood.

Q. I am not talking about your books, I am talking about the bank account.

A. There was never but one bank account, I said.

Q. This bank account was used to pay all current expenses of the business?

A. That is right.

Q. Regardless of whether or not any was left for depreciation, isn't that true?

A. I will have to have that read.

Q. You need this money in your bank account to pay the current operating expenses of your business, and you used all of that cash, if necessary, whether or not you left any for depreciation reserve? [169]

A. As long as there was any money in the bank, we would pay our bills.

Q. Now, Mr. Carpenter, you knew of course that this note that you received from the corporation was only as good as the earning capacity of that corporation?

Mr. Shearer: Just a moment. I object to that as calling not only for a conclusion but the question obviously is incorrect accountingwise.

Mr. Maiden: Your Honor, I don't care a thing on earth about accounting with this question.

The Court: Read the question.

(Testimony of Harry B. Carpenter.)

(The question was read.)

The Court: The objection is overruled. Exception allowed to the Petitioner.

The Witness: It was only as good as any money that might be in the bank to cover it, plus the protection we would have if the place failed, went into bankruptcy.

By Mr. Maiden:

Q. You say that if the corporation failed you wouldn't be entitled to take whatever cash reserve they may have had for depreciation, you would have had to share it with other creditors?

A. That is correct.

Q. You wouldn't have hesitated pursuing your claim in case of failure, to the detriment of other creditors, isn't [170] that right?

A. That is correct.

Q. Even though some of your creditors had to go without being paid in full, that wouldn't make any difference to you?

A. I don't see why they should be entitled to be paid in full any more than I. In case of bankruptcy I would lose the entire capital structure.

Q. You were responsible for the business and you had started the business and—

A. And followed—

Q. And you had incurred the debt.

A. And followed it through, to the best of my ability.

Q. Now, Mr. Carpenter, at the time this building contract was entered into in July of 1941, you

(Testimony of Harry B. Carpenter.)

knew at that time that the cost would be at least forty-four thousand-odd dollars?

A. No, I think by that time in my own mind—I don't think I discussed it with anyone; in my own mind I figured it up around thirty-eight or thirty-nine.

Q. I understood you to say you always calculated your equipment would cost about the same as the cost of the building.

A. That is correct.

Q. Well, you knew then, in July of 1941, that the [171] building would cost you at least twenty-two thousand-odd dollars?

A. I also explained that by stating we made an addition to a canopy, widened it, which increased the building cost \$4,000, but didn't have any effect on the fixtures or equipment.

Q. But the actual contract called for twenty-two thousand-odd dollars, which you knew you were going to have to pay, in July of 1941, is that right?

A. That is right. What I am trying to explain is that the building could have been built, according to the first bid, if we hadn't increased the size of the canopy, which had nothing to do with increasing the cost of the fixtures, which were setting inside the building.

Q. I am not talking about any additions that were decided to be made after you entered into this construction contract in July. If the construction contract in July called for \$22,000, then you would calculate that the cost would be at least \$44,000.

(Testimony of Harry B. Carpenter.)

A. No, because the building could have been built for \$18,000. I could have accepted the bid that he gave me of \$18,000, but I wanted to give my customers more shade, so I increased the size of the canopy.

Q. But you didn't accept that bid of \$18,000, you entered into one of twenty-two thousand-odd dollars. [172]

A. That is correct, but with an additional \$4,000 that didn't affect the fixtures in any way.

Q. I am not talking about the addition—

A. I am.

Q. —to the \$22,000. That would make it \$26,000. I am talking about the basis of \$22,000.

A. The difference between the \$18,000 and the \$22,000, Mr. Maiden, is the \$4,000; I insisted on building a wider canopy.

Q. I beg your pardon.

A. See what I am trying to get at?

Q. No. I thought that came along later on.

A. No.

Q. I believe the evidence showed that the stock certificates were not issued, at least, prior to November of 1941. A. Correct.

Q. As of that time you gentlemen knew that the cost of opening the business would approximate \$55,000? A. That is correct.

Q. Now, so far as controlling that corporation was concerned, it didn't make any difference to you from a practical standpoint whether the corporation issued 1,000 shares of stock or 7,500 shares of stock, did it?

(Testimony of Harry B. Carpenter.)

A. I will ask you to repeat that.

The Court: Read the question. [173]

(The question was read.)

The Witness: I will have to go back to the same credit proposition on the notes and the loan.

By Mr. Maiden:

Q. Well, Mr. Carpenter—

A. That was no control; no one controlled the corporation.

Q. I mean this, though: that you stockholders would have had just as effective control of this corporation by holding 10 shares apiece as you did by holding the 3,000 shares which were issued.

A. Yes, I would say we would.

Q. Now, did I understand you to say that one reason why you took part of your advances in notes was that in some of these other corporations that you were a minority stockholder?

A. I was a minority stockholder in all of them.

Q. You were a minority stockholder in this corporation? A. I was.

Q. Who was the majority stockholder?

A. There was none.

Q. Didn't you hold as much stock in this corporation as any other individual?

A. That is right. [174]

Q. And you were president of the corporation?

A. That is right.

Q. You were chairman of the board of directors, is that right? A. I think so.

(Testimony of Harry B. Carpenter.)

Q. Were you on an equal stock basis with any of the stockholders in the other corporations?

A. Well, counting Mr. Lyman and Mr. Simon as a unit, I was not, no. I probably was on an equal with some, if that is your question, but in some corporations there was no control.

The Court: Read the question.

(The question was read.)

The Court: I am not sure that is what you mean. You mean you were equal with some of them?

The Witness: I mean there may have been some stockholders in some of the corporations that didn't hold any more of the stock than I did. There were always some in the Simon corporations that held more than I held.

The Court: Proceed.

By Mr. Maiden:

Q. Mr. Carpenter, did you ever discuss with Mr. Odell the tax benefit of this type of an arrangement?

A. I don't think so. Mr. Odell and I never talked taxes. [175]

Q. Well, he was your tax man, wasn't he?

A. No, he was not.

Q. He was not? A. Not at any time.

Q. Well, I want to know whether or not you discussed with Mr. Odell, or Mr. Odell discussed with you, this arrangement, and whether or not you could get away with it.

A. No, because we had used this same thing in

(Testimony of Harry B. Carpenter.)

many instances prior to this, and there was no reason for us to think there was anything wrong with it.

Q. I believe it is stipulated in this case the Government has refused to accept this arrangement in these other corporations, and that you now have cases appearing before this Court involving this same issue, is that right?

A. I don't think in all of them; in some of them, yes.

Q. Well, the stipulation will show that.

Now, Mr. Carpenter, you say you don't know anything about the books of this corporation?

A. No.

Q. You never had known anything about them?

A. No, wouldn't know them if you showed them to me.

Q. You never did look at the books?

A. Yes, I have had them point out certain items for me. Some question might arise as to why something cost so much.

Q. Who was in charge of keeping your books in 1941? [176]

A. Well, the girl in my office, Mrs. Jennings.

Q. Mrs. Jennings, is she now with you?

A. No.

Q. How long has she been out of your employment?

A. Well, I will have to guess; I would say five or six years.

Q. Are you aware of the fact that your books

(Testimony of Harry B. Carpenter.)

during 1941 and up until Mr. Aye came into the picture in April of 1942 did not show any notes payable to the stockholders?

A. No, I don't know.

Q. You were not aware of that?

A. No. I would like to explain here, Mr. Maiden, that prior to this time that I had operated in the restaurant business since I was a youngster and that during that entire time I paid everything by cash every day, and the only checks we had to write up in our office or books we had to keep were the utilities that came in the first of the month, and the rent, and possibly some large equipment that would come in there and there wouldn't be enough cash in the register to pay for it.

With the Social Security and the increasing number of places that I was operating—this made seven at that time—it became necessary for me to change over entirely and pay on a monthly basis or semi-monthly basis and deposit all the money in the bank. This was my first experience in ever [177] carrying out anything but a cash business.

Q. Well, you had taken care of the financial operations of these other businesses by yourself then? A. That is right.

Q. You didn't keep any books?

A. I kept most of my—most of my bookkeeping was done on a checkbook.

Q. You kept that yourself?

A. I wrote all the checks and signed them myself, up until the time this other arrangement took effect, April of '42.

(Testimony of Harry B. Carpenter.)

Q. When did you discover that your books for 1941 didn't carry notes payable to stockholders?

A. Since I came in this courtroom.

Q. Since you came in this courtroom?

A. Yes.

Q. You mean to tell me that today is the very first time— A. Yesterday.

Q. Yesterday was the first time that you were apprised of the fact that your 1941 books didn't show any notes payable to the corporation—

A. That is correct.

Q. I mean to the stockholders.

A. That is correct. [178]

Q. How long have you known about the pendency of this lawsuit?

A. I don't get the word; I don't understand it.

Q. You have been in controversy with the Government— A. That is right.

Q. —about this matter for some time, haven't you?

A. Yes. Ever since the examination was made. We were notified that the Government had taken exception to this note proposition.

Q. Didn't anyone ever tell you, in discussing this matter and preparing it for trial, about the fact that your books had been changed in 1942 to show the note obligations? A. No.

Q. You didn't discuss the case with your lawyers?

A. I discussed the case very fully with my lawyers. This particular thing never came up.

(Testimony of Harry B. Carpenter.)

Q. Did your lawyers ask you to furnish them with certain facts relative to the books as they were in 1941 and as they were changed in 1942, for the purposes of entering into a stipulation with the Government?

A. No, sir. Those negotiations were all carried on with Mr. Aye's office.

Q. You mean to tell me that when you employed Mr. Aye, that he didn't tell you about this omission, if it was an omission, from the 1941 books?

A. If he told me, I can't remember it. I think I would remember it.

Q. He never discussed it with you at all?

A. The fact that the notes weren't on the book?

Q. Yes. A. No, he did not.

Q. He never told you that the entire amount of money advanced by you men to this corporation was set up as capital investment?

A. I don't think it was. If it was, I hadn't heard of it.

Q. You say you don't think it was?

A. I don't think it was set up on the books as \$55,000 capitalization.

Q. What makes you make that statement?

A. Well, I am answering truthfully what I believe to be a fact.

Mr. Maiden: Counsel, is this the same book you had here yesterday?

Mr. Webster: Yes, it is.

Mr. Maiden: Are there any pages that have been removed since yesterday?

(Testimony of Harry B. Carpenter.)

Mr. Webster: None. Can I help you?

Mr. Maiden: Yes.

By Mr. Maiden: [180]

Q. I refer you here to this page in this book that has been identified as the ledger account of the corporation, to an entry of December 31, 1941, and the name of this account is "Stock subscriptions receivable." A. Yes.

Q. I will ask you if that doesn't show a credit of \$55,000 and a charge of \$55,000?

A. That is correct. But I still don't see where it says anything in regard to capital stock or notes, either way.

Q. This says, "Stock subscriptions," doesn't it?

A. Yes, it does.

Q. I will ask you if the "55" figures haven't been marked through with a pencil and the figure "30" put above it in each instance.

A. That is correct. I also say I never saw that entry before.

Q. You never saw it before. You would say this is the first time you have seen that sheet?

A. Yes.

Q. You have never gone through this ledger sheet?

A. I didn't say that. I say at certain times I might ask questions and have them point it out to me. They are still Greek to me.

Q. In preparing this case for trial, you haven't been asked by your counsel or anyone to familiarize yourself with [181] the facts?

(Testimony of Harry B. Carpenter.)

A. The only statement I had made to me by counsel with regard to the \$55,000 was that Mr. Whittaker in error, in making out the 1941 income tax, had put it on the tax statement as \$55,000. The book was never mentioned to me.

Q. What about Mr. Whittaker's error?

A. He had made an error.

Q. Who told you that?

A. Some of my associates.

Q. Mr. Whittaker didn't tell you that?

A. No. Mr. Whittaker didn't tell me that. I said the only \$55,000 that was mentioned to me, or each time it was mentioned to me, was in connection with that 1941 income tax return.

Q. Now, Mr. Carpenter, I believe you stated that you received a note from this corporation and a stock certificate after, sometime after, the meeting that you had in Mr. Odell's office on, I believe, November 13, 1941.

A. I think I stated that I received the stock certificate and note in early December.

Q. In early December? A. Yes.

Q. Did you actually receive that note and that stock certificate in December? [182]

A. Just as true as I am sitting here.

Q. That is true of 1941? A. That is right.

Q. What did you do with your note and your stock certificate when you received it?

A. Took it directly to the safe deposit box where it remained until this week.

Q. You mean to tell me you didn't exhibit that

(Testimony of Harry B. Carpenter.)

note to the bookkeeper of the corporation for recording?

A. No, sir, didn't know it was necessary.

Q. You never did advise the bookkeeper of the corporation that you had such a note?

A. I advised my accountant.

Q. Who was that? A. Mr. Aye.

Q. When was that?

A. I don't remember.

Q. Well, it would be sometime in 1942?

A. Yes, sometime in 1942.

Q. Sometime in 1942. This note that you received bears date of November 13, 1941.

A. That is right.

Q. Was that the actual date that the note was issued, Mr. Carpenter?

A. Yes, it was the day it was issued. Whether it was [183] the day I signed it or not, I don't remember. We had our meeting, I think, on the 13th. Odell was instructed to go back and draw up the notes and issue the stock, and I think the following day my son and I went down and we both signed the notes.

Q. Well, now, when would you say that in point of time it was that Mr. Odell drew up the notes?

A. The 13th.

Q. Of November? A. Yes, sir.

Q. Well, now, in point of time, when would you say that you signed the notes? A. The 14th.

Q. The 14th? A. That is right.

Q. Now, then, you were president of the corporation and your son was secretary and treasurer?

(Testimony of Harry B. Carpenter.)

A. That is right.

Q. And the minutes of the corporation required that you and your son sign those notes?

A. Us assign them, did you say?

Q. Yes. A. No, they weren't assigned.

Q. I said "signed."

A. Yes, signed. [184]

Q. I believe there has been offered in evidence a letter bearing the signature, according to your testimony, of Mr. Odell. I believe that letter is dated December 5, 1941. Can you explain to me why it was necessary for Mr. Odell to mail you that note when, in the first place, you had to sign your own note as an officer of the corporation?

A. Well, he mailed the note, the stock certificate, and a bill for his services.

Q. I want to know why it would be that Mr. Odell would have to mail you your note when you had to sign it yourself.

A. I expect you will have to ask Mr. Odell that question.

Q. Do you have any idea why it is that Mr. Odell didn't send you that note until the purported date of December 5, 1941?

A. I wouldn't have the least idea, sir.

Q. Well, can you tell the Court that you signed this note, your own note, and then turned the note over to Mr. Odell? A. I certainly did.

The Court: Counsel, we are going to recess now until 1:45.

(Whereupon, at 12:10 p.m., a recess was taken until 1:45 p.m. of the same day.)

Afternoon Session—1:45 p.m.

The Court: Proceed with the cross examination.

Whereupon,

HARRY B. CARPENTER,

called as a witness for and on behalf of the Petitioner, having been previously duly sworn, resumed the stand and testified further as follows:

Cross Examination (Continued)

By Mr. Maiden:

Q. I believe the last question I asked you, Mr. Carpenter, was whether or not you executed your own note as an officer of the corporation and then turned it over to Mr. Odell, and I believe your answer was, "I certainly did," or that you did do that. A. I did that.

Q. Now, I wonder why it was necessary for you to turn your own note over to Mr. Odell and then have him redeliver the note to you.

A. Because in the majority of instances I left a lot of my papers with Mr. Odell, I imagine, and another thing, I don't think Mr. Odell would have permitted me to have my note until they were all made at the same time or delivered at the same time. As I explained, he was very particular in all his dealings and insisted on things that other attorneys didn't.

Q. Now, Mr. Carpenter, why was it that you issued notes [186] for only half of the amount of the advances that you made to this corporation?

A. Well, it seemed the right thing or the nor-

(Testimony of Harry B. Carpenter.)

mal thing to split it fifty-fifty. I think that had been done in the past in some of the other corporations.

Q. I believe you stated that you were interested in becoming a creditor of the corporation so that if the corporation failed, you would have a creditor's claim? A. That is right.

Q. Well, why wouldn't you have wanted to have taken as much or more of the advancement in notes rather than in stock?

A. Well, the principal idea was to have a stable corporation, one that, if it became necessary to go out in the open market and borrow money, it could be done.

Q. Well, I know, but why didn't you take two-thirds—notes for two-thirds of it, and then a third of it in stock?

A. Because it wouldn't have been as good as a bank loan had we had to borrow money from a bank, as it was with 50 per cent in notes and 50 per cent in stock.

Q. Was that the reason why you did it on the fifty-fifty?

A. That was one of the reasons, and I can't think of the rest.

Q. Well, didn't you realize that when you took 50 per cent of your advancement in notes, that that would hurt you in any credit arrangements with banks for the corporation, [187] to show those notes payable? A. I don't think it would.

Q. Well, why would it, then, if you had taken two-thirds of it in notes and a third in stock?

(Testimony of Harry B. Carpenter.)

A. Well, it seemed the right thing to do, to take 50 per cent.

Q. Well, I want to know why it seemed the right thing to take 50 per cent.

A. Well, that is the only answer I could give you, sir.

Q. Now, Mr. Carpenter, I believe you stated that you did not read the 1941 return of the corporation.

A. That is correct.

Q. But signed it without reading?

A. Or any of the other years.

Q. Or any of the other years?

A. That is right.

Q. You haven't, to this day? A. No.

Q. This 1941 return required that it be sworn to, Mr. Carpenter?

A. That is right.

Q. Did you swear to it before a notary public?

A. Yes.

Q. Do you mean to tell me that you are accustomed to swearing to things which you haven't read? [188]

A. That is prepared by people that I have my trust in, yes.

Q. Then, the statement on this 1942 return, which reads that, "We the undersigned, president or vice-president or other principal officer and treasurer or assistant treasurer or chief accounting officer of the corporation for which this return is made, being personally duly sworn, each for himself deposes and says that this return, including any accompanying schedules and statements, has

(Testimony of Harry B. Carpenter.)

been examined by him and is to the best of his knowledge and belief a true, correct, and complete return made in good faith for the taxable year stated pursuant to the Internal Revenue Code and the regulations issued thereunder.”

Then, that was not a correct statement on your part, is that correct?

A. Everything happened as exactly I told you.

Q. Well, on this return you swore that you had read the return, and now you state that you didn't read the return.

A. I didn't read the return.

Q. So then, to that extent, your oath is false?

Mr. Shearer: I object on the ground it calls for a conclusion of the witness, if your Honor please.

The Court: The objection is overruled. Exception allowed.

The Witness: Yes. [189]

By Mr. Maiden:

Q. Now, Mr. Carpenter, you stated that Mr. Whittaker left you in the spring of 1942?

A. That is correct.

Q. And I believe you gave the reason for his leaving, your dissatisfaction?

A. That is right.

Q. Now, why were you dissatisfied with Colonel Whittaker?

A. Well, in preparing the state income tax return for me which I signed and paid as I did these, he had the state tax almost as much as the federal.

(Testimony of Harry B. Carpenter.)

After he left, and I examined my copy, I called him and asked him if the state tax wasn't supposed to be approximately 25 per cent of the federal tax. His answer was that it is in most instances, but it also doesn't work out that way. So, having written the check for the large amount, I became suspicious and took my copy of the state income tax return down to a friend of mine who is also an accountant, a fellow by the name of George Temple, and Ira Thomas. Temple is Shirley Temple's father. They looked at it and—I took both the federal and the state returns down—they looked at it and recomputed it and there was an error of several thousand dollars. That was the first thing, and we had several little disagreements as we went along, and when he left, we didn't part the best of friends. [190]

Q. Well, then, at that time when you carried the state and federal returns down to this other accountant and went over it with him, didn't you discover the fact that the return reported the entire \$55,000.00 investment as capital stock on your federal return?

A. It was a prior year, it wasn't this year.

Q. It wasn't this year? A. No.

Q. Now, Mr. Carpenter, as president and chief executive officer of this corporation, didn't you feel a responsibility with respect to seeing that the books of the corporation properly reflected its operations?

A. I would have been very happy to, if I could

(Testimony of Harry B. Carpenter.)

understand them. As I explained to you, I worked on a cash basis all my life and knew no other way, and this frightened me very much when I was forced to change over to the monthly payments and sign several checks a month.

Q. Well, didn't it occur to you that you should tell your bookkeeper that this corporation had issued notes for part of this advancement and stock for the other, so that that could be recorded on the books?

A. I didn't know it was necessary to record it on the books. The books, to me, were just like the income tax returns, I couldn't understand them if I looked at them and I examined them. [191]

Q. Did you ever ask the bookkeeper to explain the books to you, to see that everything was going on the books in a proper manner?

A. I warned them many times, but I didn't ask to see the books, only in particular instances where something appeared too high.

Q. Now, Mr. Carpenter, I will ask you if it wasn't your intention prior to the issuance of this stock to issue stock of the corporation sufficient to cover the essential costs of operating the business.

A. No, it was not.

Q. It was never your intention to issue sufficient stock to cover the cost of building this drive-in and equipping it for business?

A. Never at any time.

Q. You never had that in mind?

A. Never.

(Testimony of Harry B. Carpenter.)

Q. Did you ever discuss it? A. No, sir.

Q. That you might do that?

A. No, sir; we followed the same procedure in this case that we had in previous corporations, or approximate.

Q. Now, then, Mr. Carpenter, I want to show you Exhibit 4-D to the stipulation in the case, which is an application filed with the Corporation Commissioner, and I call your [192] attention to paragraph VIII on page 3, which states, among other things, on page 4, that:

“ . . . It is proposed also to sell additional of its stock for cash and to the incorporators if it should become necessary to do so for the purpose of meeting the building or equipment or for further expanding the business or facilities thereof . . . ”

What do you know about that, Mr. Carpenter?

A. Not a thing.

Q. You never heard of that before?

A. No, sir.

Q. I will ask you if this exhibit didn't show that you signed this application for the corporation.

A. I signed the application for the corporation personally.

Q. And I will ask you if it doesn't show that you likewise filed it under your oath?

A. Yes.

Q. As appears on page 8?

A. That is correct.

Q. Now, this oath states:

“Harry B. Carpenter, being duly sworn on oath

(Testimony of Harry B. Carpenter.)

deposes and says that he is President and one of the directors of Wilshire and Western Sandwiches, Inc., a corporation, mentioned in the within application, and knows the contents thereof and that the statements [193] therein are true."

Was this just another case of your swearing to something without knowing what you were swearing to?

A. That is right, prepared by someone that I had confidence in.

Q. Now, Mr. Carpenter, I call your attention to the stipulation again, page 9, which shows the corporation Simon's Florat, the capital structure being \$10,000.00 in stock, \$38,097.09 in notes. Now, that is not split up fifty-fifty, is it? A. No.

Q. Well, why didn't you use your fifty-fifty plan in the Simon's Florat?

A. I have no answer for that. I had nothing to do with the incorporating and am not an officer or director.

Q. Well, you became a stockholder and an investor?

A. I was very happy to buy stock in any enterprise that Mr. Simon opened up, because I had the utmost faith in his ability, integrity, and brain power.

Q. Well, why did you take part of your investment in that corporation in the form of a note?

Mr. Webster: Your Honor, I will object to the form of that question, if I may.

The Court: What is the ground of your objection?

(Testimony of Harry B. Carpenter.)

Mr. Webster: The use of the word, the use of the [194] phrase, "take part of your investment in that corporation in the form of a note." This is the very issue that we are talking about.

The Court: I will sustain the objection to the question in that form.

By Mr. Maiden:

Q. Mr. Carpenter, why did you, if you were glad to have stock in any corporation of Mr. Simon's, why did you take part of your money advancement to that corporation in note?

A. Because that was the way it was set up.

Q. You disclaim any tax motive, Mr. Carpenter?

A. Yes, sir.

Q. I believe you stated you didn't even think about taxes when this plan was conceived and carried through in all these corporations?

A. I think my answer to that was that the plan would have been carried through if the tax feature wasn't there, as I remember my answer. I don't deny that I knew the tax feature was there.

Q. But did you deny that the tax feature influenced you? A. I did, because—

Q. And you now deny that?

A. I now deny that. [195]

Q. Emphatically? A. Emphatically.

Q. Mr. Carpenter, is it a fact that you were indicted in the Federal District Court in California for filing false and fraudulent individual income tax returns and false and fraudulent partnership returns for a concern by the name of Carpenter's Drive-In?

(Testimony of Harry B. Carpenter.)

Mr. Webster: Your Honor, I object to the question on the ground that it is outside of the issues of this case.

The Court: Well, of course, certain questions, even though they are outside the issues of the case, are competent for purposes of impeaching the credibility of a witness. What do you say to that?

Mr. Webster: I would like to know for what purpose the question is being asked.

Mr. Maiden: For impeachment purposes, of course.

The Court: If that is your only reason for objecting, the objection will be overruled and exception allowed.

The Witness: I was.

By Mr. Maiden:

Q. Were you convicted, Mr. Carpenter?

A. I entered a plea of nolo contendere.

Q. What is that?

A. I entered a plea of nolo contendere, if that is the correct term. [196]

Q. Did you pay a fine? A. I did.

Q. Did you receive a jail sentence or penitentiary sentence? A. I did not.

Mr. Maiden: I believe that is all, if the Court please.

Redirect Examination

By Mr. Webster:

Q. Mr. Carpenter, I show you the 1941 income tax return of the corporation, Joint Exhibit 8-H, and I ask you with respect to the fine print just

(Testimony of Harry B. Carpenter.)

above your signature on that return, which Mr. Maiden read to you, whether you read that fine print at the time you signed the return.

A. I did not.

Q. You did not? A. No.

Q. Did you know the contents of that fine print at the time you signed the return?

A. Oh, in a general way. I knew that I was signing that the return was correct.

Q. Mr. Carpenter, with respect to the oath which was attached to the application to the Corporation Commissioner for a permit to issue shares, which was previously shown to you by Mr. Maiden, had you read that? [197]

A. I read it over in a general way. I would say that I skipped through it, probably.

Q. Mr. Carpenter, you have testified to receipt of a letter from Mr. Odell, dated December 5, 1941, a portion of that letter, the last paragraph states:

“We enclose statement for services and expenses which we trust you will find entirely satisfactory.”

Is that true? A. Yes.

Q. I show you a bill from Tanner, Odell & Taft, dated December 4, 1941, and ask you if you have seen this bill before.

A. Yes, that accompanied this letter.

Q. Do you know whether that bill was paid?

A. It was, by check.

Q. Who is H. B. Carpenter, Jr?

A. My son.

Q. Do you recognize his signature?

A. Yes.

(Testimony of Harry B. Carpenter.)

Q. I ask you if this is his signature.

A. Yes.

Q. Is this the check which paid the attorneys' bill?

A. Yes.

Q. The date of this check is January 30, 1942, and the perforation date shows that it cleared through the bank on February 2, 1942. Did you understand from the contents of the bill the services which had been rendered and for which the bill was being presented?

A. I did.

Q. What did those services include?

A. It says: "For legal services in connection with incorporation permit, lease and all related matters, revenue stamps and messenger service."

Q. And that was with respect to—

A. Wilshire and Western.

Mr. Webster: I offer this as Petitioner's exhibit next in order.

The Court: Why does that have any importance to this case, counsel? I heard no objection, but I would like to know your arguments why that furthers your case.

Mr. Webster: Your Honor, Mr. Maiden asked Mr. Carpenter on cross as to the fact of whether Mr. Odell actually sent the December 4th letter—December 5th letter, 1941, on the date which the letter bore, and whether he received it in the due course of mail. Mr. Carpenter answered the question that he did receive it in the ordinary course of mail. A way of substantiating that would be to establish that the bill which was included in the

(Testimony of Harry B. Carpenter.)

letter of transmittal was actually paid a few months later.

The Court: I see. [199]

The Clerk: No. 28.

The Court: Petitioner's Exhibit No. 28 is admitted in evidence.

(The document above-referred to was received in evidence and marked Petitioner's Exhibit No. 28.)

By Mr. Webster:

Q. Mr. Carpenter, you were asked concerning a Federal and a California tax return which Mr. Whittaker had prepared, which you took down to a Mr. Temple, I believe. A. Mr. Thomas.

Q. Mr. Thomas—and both of them indicated that the State return was in error?

A. That is right.

Q. What return were you talking about?

A. My personal State return.

Q. It had nothing to do with Wilshire and Western?

A. Oh, no, this was before Wilshire and Western was organized.

The Court: You mean by that, Mr. Witness, that it was for a year prior to that?

The Witness: No, I think it was two years prior to that.

The Court: Well, when did it come up, this matter and your dissatisfaction with Mr. Whittaker?

The Witness: It started at that time. [200]

(Testimony of Harry B. Carpenter.)

The Court: The words "at that time" are still indefinite. When did your dissatisfaction arise with reference to the time of formation of the corporation which we have here?

The Witness: Well, it dated back from this State franchise return. There were some other things that came up, but I can't recall them. That one was a larger amount and remains in my mind.

The Court: Proceed.

Mr. Webster: That is all, your Honor.

Recross Examination

By Mr. Maiden:

Q. You stated that the question of the error in your State personal tax return, that your discovery of that error occurred prior to the formation of this corporation? A. Yes.

Q. I believe you stated that that was the reason why you became dissatisfied with Mr. Whittaker.

A. No, I said there were numerous things that came up.

Q. So that that wasn't the reason why you parted company with Mr. Whittaker?

A. Not entirely.

Q. In the spring of '42? A. Not entirely.

Q. Does Mr. Whittaker do the tax work for Mr. [201] McDonnell now?

A. I think not. He did at the time I started with Whittaker. In fact, that was the reason I happened to go to Mr. Whittaker in the first place.

Q. Do you have any explanation at all to offer the Court why your bookkeeper would have entered

(Testimony of Harry B. Carpenter.)

on the books of this company in 1941 the fact that this entire \$55,000.00 advance was a capital investment for which stock was to be issued?

A. I don't know it to be a fact, but I imagine Mr. Whittaker advised her to.

Q. Didn't you hear Mr. Whittaker testify that he didn't see the books, that all he did was prepare an outline and send it out to the company, and he didn't see them again until he went out to take a trial balance of all the books?

Mr. Shearer: I object to that question on the ground it misstates the evidence. Mr. Whittaker distinctly testified he recognized certain pages, if your Honor will recall, as having been typed in his office, the book which we are talking about.

Mr. Maiden: That was the opening journal entry, your Honor, that he put in there at the very first. He stated that he didn't see the other pages in the book.

The Court: Will you read the question, please?

(The question was read.) [202]

The Court: The objection is overruled.

The Witness: I don't remember what Colonel Whittaker's testimony was, all of it. I do feel confident that \$55,000.00 wasn't entered by my bookkeeper, although her initials are in there.

By Mr. Maiden:

Q. What makes you feel confident it wasn't entered by your bookkeeper?

A. Isn't it typewritten?

Q. No, it is not.

(Testimony of Harry B. Carpenter.)

A. If it is in typewriting, it wasn't entered by her, because they don't use the typewriter.

Q. Now, on this Account No. 1032, entitled "Stock Subscriptions Receivable," I will ask you if the postings in there aren't in ink.

A. That is right.

Q. You recognize that handwriting, Mr. Carpenter? A. No, I don't.

Q. Now, I will also call your attention to—

A. This handwriting here (indicating) looks very much like the lady that was working for me in the beginning, but this (indicating) doesn't.

Q. Now, I will also call your attention to Account No. 302.

The Court: Now, Counsel, I call your attention to [203] the fact that the word "this" is very indefinite, and just from hearing the words "this is" so and so and "this is" so and so, I won't know what that testimony means.

By Mr. Maiden:

Q. Coming back to Account No. 103, under date of 1941, being put in in ink, under that December 31 in ink, posting reference J-3 in ink, and under word "Credit," \$55,000.00, and then likewise, December 31, ditto for posting reference in ink, \$55,000.00. Now, do you know whose handwriting that is? A. No, I do not.

Q. You do not?

A. As I say, these initials by the side of it look like her handwriting, but the words "Post for credit, refund of excess profits tax," don't look like her handwriting. It could be.

(Testimony of Harry B. Carpenter.)

Q. I believe the "55" in each one of these figures of \$55,000.00" has been marked through with a pencil and, in pencil, "30" has been entered above the "55", is that right? A. That is right.

Q. Now, calling your attention to Account No. 302 in this ledger book that has been identified as being the ledger book of the corporation, designated "Stock Unissued," I will ask you if this doesn't bear an entry under 1941, March 24, and under the column "Charges," \$75,000.00, and then if under [204] that it doesn't bear the date December 31, and following that, \$55,000.00, which has been run through with an ink mark, and if under the column "Credits" \$55,000.00 doesn't appear in ink, and the "55" has been marked through and "30" put above it. A. That is right.

Q. I will ask you if, under the column "Balance," there isn't a figure in pencil of \$45,000.00.

A. That is right.

Q. Do you know whose handwriting that is?

A. No, but I imagine it is Mrs. Jennings, my bookkeeper.

Q. You have no explanation to offer as to how she could have made those entries?

A. No, unless Mr. Whittaker advised her to. That is the general procedure in my office, for the auditor to have the bookkeeper enter them in the ledger, or the accountant do it himself.

Q. Did you have an auditor at that time, in 1941? A. I had Mr. Whittaker.

Q. Well, I understood Mr. Whittaker to testify that he was not in charge—

(Testimony of Harry B. Carpenter.)

A. I am in error. I guess I called him in as an auditor on Wilshire and Western.

Q. Simply for the purpose of setting up—

A. A set of books. [205]

Q. Set of books?

A. Which, by the way, is the first set of books I ever had.

Q. I believe Mr. Whittaker testified, in addition to typing the opening statements in your journal, that he sent you a list designating the entry number, account number, and the title of the account, and that that is all he had to do with the books.

A. That I don't remember. Now, I think he said—

Mr. Shearer: Just a minute, please. I object to the question, which is not a question but simply a statement of what Colonel Whittaker was supposed to have testified to and which is a matter of record here.

Mr. Maiden: Your Honor, I have got a right—

The Court: The objection is overruled; exception is allowed.

The Witness: I think he said his son came out and typed some pages in the ledger.

By Mr. Maiden:

Q. What?

A. I think he said his son came out and typed some pages in the ledger. I don't remember his son ever coming out, but that is what he stated and probably is true.

Q. Of course, his testimony is in the record, and I may have been wrong about it. [206]

(Testimony of Harry B. Carpenter.)

A. Well, I am sure he mentioned his son.

Q. I believe he stated that his son took off the trial balance?

The Court: Well, let's not discuss the evidence any further. It is there for whatever it states.

Mr. Maiden: I believe that is all, if the Court please.

The Court: Anything further from this witness?

Mr. Webster; Nothing, your Honor.

The Court: Do both sides agree to excuse the witness from further attendance in this case?

Mr. Maiden: As far as the respondent is concerned.

Mr. Webster: Yes.

The Court: You are excused from further attendance.

(Witness excused.)

Whereupon,

ELIAS J. AYE,

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you tell us your name?

The Witness: Elias J. Aye.

Direct Examination

By Mr. Webster:

Q. Mr. Aye, what is your occupation? [207]

A. I am a member of the California State bar and a certified public accountant.

(Testimony of Elias J. Aye.)

Q. How long have you been in practice?

A. Since—in law practice?

Q. Well, let's break it down, then. How long in law practice?

A. Well, I was admitted to the State bar in 1913 and I passed the C.P.A. examination in 1918.

Q. Are you in the active practice of both of those professions at the present time?

A. Well, I would say I am retired. I still do a little work.

Q. Were you active in 1941? A. Yes.

Q. We have had testimony to the effect that a client of yours in 1942 for accounting purposes was Wilshire and Western Sandwiches, is that correct? A. Yes.

Q. When did you first commence working with them as a client?

A. I believe it was April or May, 1942. It was after the tax season, I know that.

Q. Can you recount for the Court the circumstances under which you acquired Wilshire and Western Sandwiches as a client? [208]

A. William H. Simon and Mike Lyman, clients of mine since about 1918 or '19, and Mr. Simon told me that he wanted me to go out and take a look at this Wilshire and Western set of books and see what they had, that he didn't have confidence in the man they had out there, and he wanted to know what was on the books.

Q. Did he mention to you the name of the man whom they had out there?

A. Yes, I think he did.

(Testimony of Elias J. Aye.)

Q. Do you remember the name?

A. Colonel Whittaker.

Q. You say you went out there in April or May of 1942? A. Yes.

Q. What was the first thing which you did when you got out there?

A. Well, I imagine the first thing I did was to try to get a trial balance on the general ledger.

Q. Do you recall as of what date?

A. No, I wouldn't recall that now.

Q. Was it around the time at which you went out there?

A. Yes, it was a current trial balance.

Q. Do you recall the results of that attempt to take a trial balance?

A. Well, being acquainted with Mr. Simon's business, I knew that he had taken notes from the Wilshire and Western [209] Sandwiches—Wilshire and Western Corporation—and they showed no notes on the books at all. I knew that all of the contributors to the stock out there had notes, too.

Q. Having found that out, what was your next step?

A. Well, I went back and talked to Mr. Simon and talked to Mr. Carpenter and they agreed that it was wrong, and to dig into it and straighten it out.

Q. Did you attempt to take a trial balance at an earlier date?

A. Well, they had a trial balance at an earlier date.

Q. What date was that?

(Testimony of Elias J. Aye.)

A. Well, they had the trial balance at the end of the previous year.

Q. That would be December 31, 1941?

A. Yes.

Q. I believe these are your working papers which you used in connection with your work at Wilshire and Western, is that correct?

A. Yes, that is correct.

Q. Did you personally prepare those working papers?

A. Yes, these are in my own handwriting.

Q. You stated you took a trial balance as of December 31, 1941. What was the result of that trial balance?

A. Well, the trial balance did not reflect the notes which the corporation had issued. It misstated the amount of [210] capital stock outstanding.

Q. Can you see anything else in that trial balance which was in error?

A. Yes. They had a number of refunds shown as income, and I asked Mr. Carpenter how a concern just starting in business could have a lot of refunds, what they were from, and I finally got him to spend enough time with me to look at them, and he said, "Oh, those are in connection with the business which I had on the old stand. Those are mine. They don't belong to this corporation."

I said, "All right, I will take them out."

Q. Is that what you did?

A. Yes. Then I set up the notes and set the

(Testimony of Elias J. Aye.)

capital stock up the way the stock had been issued in accordance with the permit from the Corporation Commissioner.

Q. Did you examine the 1941 tax return which had been filed? A. Yes.

Q. That is, the retained copy of it?

A. Yes, sir.

Q. What did you conclude with respect to its accuracy?

A. Well, it was inaccurate as to the things which I mentioned, and I prepared an amended return and filed that with the Collector of Internal Revenue, and a copy with the State Franchise Tax Commissioner. [211]

Q. Do you recall the manner in which you filed the amended return with the Collector of Internal Revenue?

Mr. Maiden: Has he testified that he did file one?

Mr. Webster: Yes, he did.

The Court: He stated he did, a moment ago.

Mr. Maiden: All right.

The Witness: I mailed it in, my office mailed it in.

By Mr. Webster:

Q. Mr. Aye, I show you a 1941 "Corporation Income and Declared Value Excess-Profit Tax Return," which is in pencil, and ask you whether you can identify the handwriting.

A. Yes, that is my handwriting.

Q. The statement at the top of the form reads, "Amended return," is that your handwriting?

(Testimony of Elias J. Aye.)

A. Yes, it is.

Q. Do you recall preparing this form?

A. Very well.

Q. Do you recall the date at which you prepared this form?

A. Well, it was possibly May of 1941.

Q. May of 1941? A. '42, pardon me.

Q. Mr. Aye, I show you a typewritten form of 1941 "Corporation Income and Declared Value Excess-Profit Tax Return," and ask you whether you can identify this form. [212] A. Yes.

Q. What would you say it is?

A. Well, that is a corporation income tax return for the year 1941, and it was typed on a machine which we had in our office.

Q. You recognize the type of the typewriter?

A. Yes, it is an unusual type.

Q. From inspection, does it accord with the pencil copy of the return which you have?

A. Yes.

Q. Was it a duplicate or replica of this typewritten return which was sent in the mails by you to the Collector of Internal Revenue?

A. Yes, this is our retained copy.

Mr. Webster: I will offer the penciled 1941 tax return as Petitioner's Exhibit next in order.

Mr. Maiden: Your Honor, I would appreciate very much if counsel would simply offer it for identification at this time and give me an opportunity to examine Mr. Aye before stating I have no objection.

Mr. Webster: Very well, your Honor.

(Testimony of Elias J. Aye.)

The Court: Identify the instrument.

The Clerk: It is identified as No. 29.

(The document above-referred to was marked
Petitioner's Exhibit No. 29 for identification.)

Mr. Webster: I offer the typewritten 1941 corporation amended return—

Does your same request apply to this?

Mr. Maiden: Yes, but it would seem to me that one would do the trick, though. I don't see the sense of putting both in.

Mr. Webster: Just for identification.

The Clerk: It will be No. 30.

The Court: It will be marked for identification as Exhibit No. 30.

(The document above-referred to was marked
Petitioner's Exhibit No. 30 for identification.)

By Mr. Webster:

Q. Mr. Aye, Exhibit 8-H has been identified as the original 1941 tax return which had been prepared by Mr. Whittaker. The amount of normal taxable net income shown on this return is \$5,094.88. I ask you whether you can locate that amount in the general ledger of Wilshire and Western Sandwiches.

A. Yes, it is here in the journal in someone else's handwriting.

Q. Do you know whose handwriting it is?

A. No, I don't, but the entry in the ledger is in my handwriting.

Q. What entry is that? [214]

A. Setting up this earned surplus which Colonel Whittaker showed.

(Testimony of Elias J. Aye.)

Q. Do you recall whether there was a ledger sheet entitled "Earned surplus," prior to the time of your commencing to work for Wilshire and Western Sandwiches?

A. I think there must not have been.

Q. Do you know whose handwriting—

A. That is my handwriting.

Q. You are speaking now of the words "Earned surplus"? A. Yes.

Q. Under the word "Capital" in the ledger?

A. Yes.

Q. At the top of the page, that handwriting is yours? A. That is right.

Q. Would you describe for the Court the significance of the next entry underneath the entry of \$5,096.88, which you have stated you incorporated in the earned surplus ledger?

A. Those are the correcting entries which I made to take out the miscellaneous receipts and make the other adjustments necessary to have Colonel Whittaker's trial balance reflect the transactions according to the minutes of the corporation, and according to the true nature of the miscellaneous receipts.

Q. Does the second entry under the earned surplus ledger refer to these papers under the tab "Journal" appearing on [215] pages 4, 5, and 6?

A. Yes.

Q. Are these pages 4, 5, and 6 under the tab "Journal" in a handwriting familiar to you?

A. They are in my handwriting.

Q. They are in your handwriting?

(Testimony of Elias J. Aye.)

A. Yes.

Q. Do you recall when you made this journal entry of which we are speaking, that is, J-4, -5, and -6? A. Possibly in May, '42.

Q. Can you find in the "Earned surplus" ledger an account, or in J-4, -5, and -6, the amount of the net income, normal taxable income, which you arrived at as proper for the year 1941 for the corporation? A. Yes, it is this \$2,468.16.

Q. This amount corresponds with the amount on the tax return which you have previously identified? A. Yes.

Q. Mr. Aye, are you familiar with the adjustments which were made by the revenue agent in the 1941 tax return of the corporation?

A. In a general way. I didn't handle that personally.

Q. Have you ever seen a copy of the 90-day letter which was issued by the Internal Revenue service of the Treasury Department on January 31, 1946? [216]

A. No, I think I never have seen this.

Q. On page 3 of the 90-day letter is the statement that the net income adjusted for the taxable year ended December 31, 1941, is in the amount of \$2,237.18.

A. Well, I think I will have to change my answer.

Mr. Maiden: If your Honor please, I object to this witness testifying from that document. He has stated that he has never seen it before. I just don't understand the purpose of it. It relates to the taxable year 1944.

(Testimony of Elias J. Aye.)

Mr. Webster: What relates to the taxable year 1944?

Mr. Maiden: This 90-day letter I thought you were referring to relates to 1941, doesn't it?

Mr. Webster: Yes. If we are going to exclude everything that related to the calendar year 1941, we would have stricken a lot of this testimony.

Mr. Maiden: Well, if your Honor please, the tax liability of this petitioner for the year 1941 is not before the Court in this proceeding. I haven't caught the possible materiality of this examination.

Mr. Webster: If your Honor please, the abilities, the respective abilities, of the accountants employed by Wilshire and Western Sandwiches, have apparently been placed in issue.

Mr. Maiden: The respectabilities?

Mr. Webster: Respective abilities. [217]

Mr. Maiden: I haven't so conceived any such issue in this case.

Mr. Webster: Well, our claim was, and was made at the outset—

The Court: Just direct your objection to me and not to each other. I don't want a harangue and soliloquy between you, on the part of either one of you, or between you.

Mr. Webster: If your Honor please, our contention is that the original return filed by Mr. Whittaker was in error; that the amended return—

The Court: For 1941?

Mr. Webster: For the calendar year of 1941; that an amended return was filed; that this amended return corresponds within two hundred dollars or

(Testimony of Elias J. Aye.)

thereabouts of the amount which the revenue agent conceded to be correct, and that this in turn reflects upon the abilities of the accountant who was originally employed by the petitioner in this case.

The Court: Well, that is going pretty far, but I will not stop you. The objection is overruled.

By Mr. Webster:

Q. Mr. Aye, are you able to reconcile the \$2,237.18 of the 90-day letter with your \$2,468.16?

A. Not exactly, but—

If your Honor please, the reason I said I thought I [218] would have to change my answer about never having seen this before, in my own handwriting I have an amount written here which the agent shows, so I have seen it before.

Q. And with respect to the reconciliation of the two amounts, would you offhand be able to give us a reconciliation? A. Not offhand, no.

Q. Mr. Aye, it is evident one of the differences between the original tax return filed by Mr. Whittaker and the amended return which you have stated you filed, as found on the balance sheet, page 4 of the return—would you describe the nature of the difference found therein?

A. Colonel Whittaker set up the entire amount of money advanced by the stockholders for which they took notes, and for which they took stock, all as common stock. On the balance sheet which I set up, I showed \$30,000.00 capital stock and \$25,000.00 notes payable.

Q. Did you ever see the stock certificates?

A. Yes, I have seen the stock book.

(Testimony of Elias J. Aye.)

Q. You have seen the stock book?

A. Yes.

Q. Where did you see the stock book?

A. In Mr. Odell's office.

Q. Did you see any other corporate records?

A. I saw the minute book, also the stock book.

Q. When was it that you saw those?

A. When I made these changes, along, in, possibly, 1942.

Q. Did you ever see any notes of the corporation referring to either or some or all of Mr. Lyman, Mr. Simon, Mr. Carpenter, or Mr. McDonnell?

A. I know that I saw Mr. Simon's and Mr. Lyman's notes.

Q. You saw those?

A. Yes, that is how I knew this couldn't be.

Q. Mr. Aye, I wonder if you could clarify the penciled corrections to which reference has previously been made, found in Account No. 1032, the title of that account is "Stock Subscriptions Receivable."

A. Yes, those are my changes.

Q. The penciled changes are yours?

A. Yes.

Q. You are referring to a line in pencil drawn through the digits "55" and a number "30" written above?

A. Yes.

Q. Can you explain the circumstances surrounding the making of this correction?

A. This Account 1032 is "Stock Subscriptions Receivable." Whoever set this up, Colonel Whitaker or the bookkeeper, set up \$55,000.00 as stock

(Testimony of Elias J. Aye.)

subscriptions receivable, and according to the minute book and to the word of the attorney and the stockholders, it was only \$30,000.00. [220]

Q. Was it for this reason that you made the change? A. Yes.

Q. There is a posting reference opposite each one of these changes on Account No. 1032, to J-3?

A. Yes.

Q. Would you describe for the Court what you find on J-3?

A. J-3 shows a debit to stock subscriptions receivable of \$30,000.00, a credit to capital stock unissued of \$30,000.00, the original entry in both instances was \$55,000.00.

The Court: Mr. Aye, will you keep your voice up a little more, please?

The Witness: I am sorry, sir.

By Mr. Webster:

Q. The original entry you say was \$55,000.00. Do you know in whose handwriting that was?

A. No, I do not.

Q. Do you know whose handwriting made the correction?

A. That is my handwriting that made the correction.

Q. Can you place in point of time the making of this correction and the making of the correction in the Account No. 1032?

A. Well, they would be made together.

Q. All of this you have previously said you did about in May of 1942? [221]

A. That is correct.

(Testimony of Elias J. Aye.)

Q. I call your attention to Account No. 203. This account is entitled, "Advances by stockholders," and I ask you to explain to the Court what you find on that page.

A. It says "Wilshire and Western Sandwiches, Inc., Advances by stockholders," and it says, "Journal." It doesn't say which one. It must be Journal 4. I have a credit of \$25,000.00.

Q. The first credit is a credit of \$25,000.00?

A. Yes.

Q. Do you know whose handwriting that is in?

A. That is my handwriting.

Q. You have stated that the posting reference is to what? A. It is to J-4.

Q. Posting reference is to J-4. At the top of the J-4 is printed "Record of journal entries, month of"—interlined between "of" and "journal" is a word "correcting", which is in pencil. Do you recognize that handwriting?

A. Yes, that is my handwriting.

Q. And written in pencil is the date "December 31, 1941." Do you recognize that handwriting?

A. Yes, that is also my handwriting.

Q. Now, at the bottom of the page is a journal entry stating "Capital Stock, \$25,000.00 charged, and Notes [222] Payable, \$25,000.00 credit," with the legend, "To correct amount shown as capital stock issued and credit Notes Payable for difference."

Do you recognize that handwriting?

A. That is my handwriting.

(Testimony of Elias J. Aye.)

Q. You have previously stated that this page was written by you at about the same time as the other pages were corrected, is that true?

A. That is correct, these are my corrections, my correcting entries.

Q. It is this journal entry you state to which the first entry in Account 203 refers?

A. Yes.

Q. Would you kindly describe for the Court the second entry?

A. The second entry is dated February, 1942, and it says, "Bank deposit, also a credit of \$10,000.00."

Q. Do you know whose handwriting that is?

A. That is my handwriting.

Q. Can you explain what that would refer to?

A. That would be an additional \$10,000.00 advanced to the corporation by the stockholders.

Q. At what time? A. In February, 1942.

Q. Would you briefly explain to the Court what the [223] contents of the remaining entries on the page, Account No. 203, show?

A. The next entry bears the date of September 30, 1942. The posting reference is the checkbook 21, and a charge for \$10,000.00, which would indicate that \$10,000.00 had been repaid to the notes payable.

Then, the next entry is 1943, April—

Q. Pardon me, may I interrupt, Mr. Aye? Do you recognize this handwriting of the entry which you previously described?

A. No, I do not. It must be the bookkeeper at Carpenter's.

(Testimony of Elias J. Aye.)

Q. Continue.

A. The next entry is April, 1943, April 30th, check register 14, a debit of \$9,998.99.

Q. Do you recognize that handwriting?

A. That is Mr. Tompkins' handwriting.

Q. Mr. Tompkins is who?

A. Mr. Tompkins is a certified public accountant who has been associated with me for a great many years, and he took charge of the handling of this account after I had made the first entries and we had threshed it around. He ran it from then on.

Q. Would you explain to the Court the significance of this entry which you just read? [224]

A. That would mean that the corporation had returned \$9,998.99 to the notes, they paid that much on the notes to the stockholders.

Q. Would you read the next entry?

A. The next entry is made on May 31, 1944, and then in pencil after it is written "May 23," which is probably the date that the checks were dated.

Check register 65, \$10,001.01.

Q. Do you recognize that handwriting?

A. That is Mr. Tompkins' handwriting.

Q. And the significance, I take it, would be the same as the previous one?

A. That was an additional payment on the notes.

Q. Would you finally explain the last entry on the page?

A. The last entry is March 31, 1945, check reg-

(Testimony of Elias J. Aye.)

ister 11, \$5,000.00, which paid off the balance on the advances by stockholders.

Q. And that handwriting?

A. That is Mr. Tompkins'.

Q. Turn to Account No. 302, which is titled "Capital Stock Unissued," and I ask you to explain briefly to the Court what you find on that page.

A. The opening entry on this account was a debt of \$75,000.00. [225]

Q. Do you recognize that handwriting?

A. No, but it is the same handwriting that made the other opening entries. I don't know who it is.

Q. The posting reference is——

A. The posting reference is J-2.

Q. And J-2, I believe, has been previously identified as the typewritten journal entry prepared by Mr. Whittaker in his own office?

A. That is correct.

Mr. Maiden: Just a second, counsel——

By Mr. Webster:

Q. Would you kindly explain to the Court the significance of the next entry you find on Account No. 302?

A. There had previously been an entry made, a credit of \$55,000.00, which I changed to \$30,000.00 for the same reason that I changed the capital stock issued.

Q. The correction is in your handwriting?

A. Yes.

Q. Do you remember when you made that correction?

(Testimony of Elias J. Aye.)

A. The same time I made the other corrections.

Q. Can you recall any other adjustments which you made with respect to the stock and loan accounts, other than the ones which we just discussed?

A. I think that is all of them.

Q. Mr. Aye, I show you the 1942 tax return filed by [226] Wilshire and Western Sandwiches, and ask you whether you know who prepared that return.

A. Yes, that was prepared in our office.

Q. Is this your signature on the return?

A. This is my signature, yes.

Q. I call your attention to the balance sheet on the reverse side of the tax return prepared by you for the calendar year 1942. Would you kindly read to the Court the loan payable and capital stock entries that are made on that balance sheet?

Mr. Maiden: If the Court please, that return is in evidence and I think it is wasting the time of the Court to have him read off figures that appear on the balance sheet of the return which is in evidence.

The Court: We have been going into an awful lot of detail here, counsel. Why is it necessary to repeat what is in the record?

Mr. Webster: If your Honor please. I was about to ask the witness whether the reason that he prepared this 1942 return in the manner in which he did stemmed from the corrections which he made in the books.

The Court: The objection is overruled.

(Testimony of Elias J. Aye.)

Mr. Webster: Would you read the question?

(The question was read.)

The Witness: The loans payable were \$25,000.00, [227] both at the beginning and the end of the period. The capital stock was \$30,000.00 at the beginning and the end of the period.

By Mr. Webster:

Q. Were those entries on that balance sheet the result of corrections which you had made on the books of Wilshire and Western?

A. Yes, it was changed from \$55,00.00 to \$30,000.00.

Q. I show you the balance sheet on page 4 of the 1943 income tax return, and ask you to read for the Court the same entries or corresponding entries.

A. At the beginning of the year, the loans were \$25,000.00, the stock was \$30,000.00. At the end of the year the loans were \$15,001.01, the capital stock \$30,000.00.

Mr. Webster: Your Honor, at this time I should like to introduce into evidence the ledger of Wilshire and Western Sandwiches, making a motion at the same time to withdraw the same for the purposes not only of writing the brief, but for the purposes of enabling the corporation to make appropriate entries, and the right to substitute in evidence photostatic copies of all pages of the ledger accounts with respect to which we have had testimony at any time during this proceeding.

The Court: Is there any objection?

(Testimony of Elias J. Aye.)

Mr. Maiden: No objection, your Honor, except I do [228] want to be furnished with a copy of the exhibit, that is, a copy of the photostatic copies, and I would also like to have the privilege of determining which entries are to be photostated and which are not.

Mr. Webster: That privilege certainly will be granted, your Honor. At the same time I should like to request that photostatic copies of the tax return be furnished to the taxpayer.

The Court: Well, neither side has an absolute right to copies of the exhibits. The exhibits are before the Court when they are introduced in evidence, and it is just a matter of courtesy between you, now, as to whether you are going to furnish the other person a copy.

Mr. Maiden: Well, your Honor, I object to this journal going into evidence with the right of counsel to supply photostatic copies of certain pages without the understanding that I likewise will have the right to submit photostats of any of the entries in the journal that I think might be pertinent in the case.

Mr. Webster: That is perfectly all right.

The Court: Of course, I will give you both that privilege if I give it to either one of you. The ledger is admitted into evidence. Both sides will be given permission to substitute a photostatic copy for any pages that have been referred to in evidence and which either counsel sees fit. [182] It will be admitted into evidence as Exhibit No. 31.

(Testimony of Elias J. Aye.)

(The document above-referred to was received in evidence and marked Petitioner's Exhibit No. 31.)

Mr. Webster: No further questions, your Honor.

Cross Examination

By Mr. Maiden:

Q. Mr. Aye, who was it who asked you to take over the corporation's books?

A. Mr. Carpenter.

Q. Mr. Carpenter? A. Yes.

Q. When was that?

A. Oh, it was early in 1942. I don't remember the exact date.

Q. Did you immediately go out to the plant and go over the books?

A. No, I couldn't do it right at the time.

Q. Well, what was the occasion for your going out there when you did, in April or May?

A. Well, it was just like another job, I had to go out and do it, I was asked to do it.

Q. What did you go out there to do?

A. To see that the books were properly set up and that they were properly being kept.

Q. Did Mr. Carpenter indicate to you that he didn't [230] know whether the books were being kept properly? A. No.

Q. He didn't tell you, then, that he thought the books had been kept improperly and he wanted you to go out and straighten them out?

(Testimony of Elias J. Aye.)

A. He wanted me to go out and take charge.

Q. Well, Mr. Carpenter had a bookkeeper, didn't he, keeping his books currently?

A. He had had a bookkeeper for a great many years whom I never met, this Mrs. Jennings that he spoke of. He had a new bookkeeper when I got there.

Q. Was that a man or a woman?

A. That was a woman. She defaulted on some of her funds.

Q. Which bookkeeper defaulted?

A. The new one.

Q. The new one? A. Yes.

Q. Do you know when the new one was employed?

A. She was there when I went out there.

Q. She wasn't the bookkeeper that had been there at the end of 1941? A. No.

Q. Did you ever contact the bookkeeper who kept the books in 1941? [231]

A. No, I have never seen her.

Q. You have never seen her. Well, when you got out there to the plant, what did you do first?

A. I tried to find out what they had on their books. You usually start in with the general ledger.

Q. Is that what you did in this case?

A. I imagine so.

Q. Then, after you went through the general ledger, did you see anything wrong with the general ledger?

A. Yes. They didn't have any notes payable.

(Testimony of Elias J. Aye.)

Q. Well, had you previously been advised that there were some notes payable that had been issued?

A. Yes, I knew about those because, as I said before, Mr. Simon and Mr. Lyman had been clients of mine for many years, and I knew that they had some notes from this corporation.

Q. Well, how did you happen to know that they had some notes from this corporation, Mr. Aye? A. They had the notes.

Q. Well, what was the occasion for their showing you the notes?

A. I also saw all of those things. If they brought stock, I saw it.

Q. Well, before you went out to the plant?

A. No.

Q. I thought I understood you to say that Mr. Carpenter [232] asked you to go out and take charge of the books and go over the books.

A. He did. I think it was Mr. Simon's idea, but, of course, Mr. Carpenter had to ask him before I could.

Q. But before you went out there, they told you they had notes of the corporation?

A. Yes, I knew that when I got there. I knew they had stock in the corporation, I saw that their records were kept.

Q. Oh, you kept Mr. Simon's and Mr. Lyman's records, is that right?

A. I looked at them, yes.

Q. For their personal returns or corporation

(Testimony of Elias J. Aye.)

returns? A. Both.

Q. Both. For some of Mr. Simon's corporations, is that right? A. All of them.

Q. You had seen some notes that Mr. Simon and Mr. Lyman had, as well as some stock?

A. Yes.

Q. In this particular corporation?

A. That is true.

Q. Now, did they tell you that those notes hadn't been set up on the books?

A. They didn't know that. [233]

Q. They didn't know that. I believe you stated on direct examination that Mr. Carpenter likewise told you that he had some notes, is that right?

A. Well, I knew about the situation. I don't remember whether it was Mr. Carpenter that told me or Mr. Simon told me.

Q. Well, I believe you did state on cross examination that when you went out there and found that there weren't any notes on the books, that you went to Mr. Carpenter and Mr. Simon both and asked them about it, is that right?

A. That is correct.

Q. And that you asked them whether this was the way it should be or whether it should be set up with the notes as loans, and that they told you that the books had been set up wrong?

A. I don't believe I said that.

Q. Well, just what did you say?

Mr. Shearer: I object——

Mr. Maiden: Just a minute, I am asking what he did say.

(Testimony of Elias J. Aye.)

The Witness: I reported to them that the books didn't show any notes.

By Mr. Maiden:

Q. Well, I believe you stated something about asking them if that was correct, and they said that was wrong. [234]

A. I don't think I said that.

Q. You talked to Mr. Carpenter about it?

A. Yes.

Q. You explained to Mr. Carpenter that the notes didn't show upon the books?

A. Yes.

Q. And explained to him that the entire advancement had been set up to capital stock?

A. Had been set up as advances by stockholders.

Q. Well, had been set up as chargeable to capital stock to be issued? A. That is right.

Q. Now, Mr. Aye, you are not undertaking to tell this Court that those notes were in fact bona fide loans rather than investments, are you? I mean, you have no personal knowledge of that, yourself?

Mr. Webster: If your Honor please, I request the question be read.

The Court: Read the question.

(The question was read.)

The Witness: Yes, I have personal knowledge of that. I was present when they talked about it, when they discussed it.

(Testimony of Elias J. Aye.)

By Mr. Maiden:

Q. When was that, Mr. Aye? [235]

A. Oh, that was when they were going into this deal.

Q. You mean you were present when these men discussed the formation of this corporation?

A. Yes.

Q. Did you hear them discuss the capital structure of this corporation? A. Yes.

Q. Did you participate in the discussions?

A. Well, I never had much to say, but they used to have me come in and sit in the office a lot of times.

Q. You weren't working for this corporation, though? A. I was working for Mr. Simon.

Q. Working for Mr. Simon. Did you hear him say—explain why they wanted to take notes for part of the advancement rather than take it all in stock?

A. Yes, as they said here, they wanted to be——

Q. I don't care what they said here. I want to know what they said in this conference that you attended with them.

A. Well, they said they wanted to take part of it in stock and part in notes.

Q. Well, did they say why?

A. Yes, they could get the money back for the notes.

Q. Have you been present during the testimony of Mr. Carpenter and Mr. Simon?

A. Yes. [236]

(Testimony of Elias J. Aye.)

Q. You heard them testify in this case?

A. Yes, I did.

Q. Did you hear them say anything about the tax benefit of this arrangement?

A. Yes, I think they discussed that, too. Of course, the tax benefit is apparent.

Q. Did you request Mr. Carpenter to read the amended return, which you say you prepared for 1941?

A. Yes, I gave it to him, but he didn't read it.

Q. Is it customary for you, in your preparation of tax returns, to request that the client read the return and discuss the return with you?

A. Yes. Some of them do, but most of them don't.

Q. Now, Mr. Aye, you state that you prepared an amended return for 1941, and you stated that you filed that return, is that right? A. Yes.

Q. Did you personally file it?

A. I think it was mailed from the office.

Q. Do you have personal knowledge of the fact that that return was mailed from your office?

A. Well, that would be the ordinary course of business.

Q. Well, I am asking you now, do you know in this case as a matter of fact that that return was mailed to the Collector of Internal Revenue?

A. I didn't mail it myself, I don't imagine.

Q. So you don't know as an actual fact whether it was mailed?

A. At the same time we made out a return to

(Testimony of Elias J. Aye.)

the State Franchise Tax Commissioner; we got a letter back about that one.

Q. Did you get a letter back about the filing of an amended 1941 return from the Federal Government? A. No.

Q. All you know is that you prepared this return, this amended return?

A. Yes, prepared it, and I know that it was filed.

Q. Well, now, just tell me how you know it was filed if you didn't file it physically and you didn't mail it?

A. Well, it is the ordinary procedure, it is the ordinary course of business.

Q. Well, you are just assuming that you followed the ordinary course of business in this case?

A. That is correct.

Q. Did you prepare any claim for refund?

A. Yes, I believe I did.

Q. When did you prepare those?

A. I think it was filed at the same time.

Q. The same time? A. Yes. [238]

Q. Are you sure of that?

A. I should think that an 843 would be filed at the same time, yes.

Q. In filing the returns through the mail with the Collector of Internal Revenue, did you usually accompany the return by a letter of transmittal?

A. No, sir.

Q. What did you do, just put them in an envelope? A. Yes.

(Testimony of Elias J. Aye.)

Q. That is always your practice?

A. Well, in the rush season, I will send them up with a list and get a receipt for it, when they are throwing them in baskets and on the floor, and places like that, but in an odd return like this, filed by itself, I just mail it to them.

Q. You didn't accompany it with any letter of transmittal? A. I don't think so.

Q. As a matter of fact, I believe you stated that you didn't put the return in an envelope and mail it, address it—

The Court: Haven't we gone over this often enough? This man has said in effect a long time ago—it has been quite obvious—that he didn't know positively, and he said he relies upon his course of business. Let's not run this thing threadbare.

Mr. Maiden: Yes, sir. [239]

By Mr. Maiden:

Q. Now, Mr. Aye, all the changes that you made on the books there in the spring of 1942 were changes made to reflect or to show the advancements made by the organizers and stockholders as an investment of \$30,000.00 and loans of \$25,000.00; is that correct? A. Yes.

Q. You opened such other entries in the books as were required by that change? A. Yes.

Mr. Maiden: I believe that is all, if the Court please.

The Court: Is there anything further of this witness?

Mr. Webster: Nothing further, your Honor.

The Court: Mr. Aye, I have been wondering

(Testimony of Elias J. Aye.)

why, since you represented, as I understand you to say, Mr. Simon and Mr. Carpenter in 1941 in their personal income tax matters, and you being a tax man, I am wondering why you were not used originally to set this matter up rather than Colonel Whittaker.

The Witness: I think you misunderstood me. I said that I was—I made the returns for Mr. Simon and Mr. Lyman, who is Mr. Simon's brother.

The Court: Not for Mr. Carpenter? [240]

The Witness: Not for Mr. Carpenter. Mr. Carpenter was in charge of this corporation, so he had this man do it.

The Court: I see. Mr. Carpenter was in charge, and he had his own man do it, and you were not called upon to do this work in 1941?

The Witness: Yes, sir.

The Court: That is, the corporate work.

The Witness: The corporate work I had nothing to do with until 1942.

The Court: That is all I want to ask.

Mr. Webster If your Honor please, I have overlooked that Petitioner's Exhibits 29 and 30 for identification have not been introduced, and I offer them in evidence at this time.

The Court: Petitioner's Exhibits Nos. 29 and 30 are admitted in evidence.

(The documents heretofore marked Petitioner's Exhibits Nos. 29 and 30 were received in evidence.)

Mr. Webster: That is all, your Honor.

The Court: Is this witness being excused by both sides?

Mr. Webster: Yes, your Honor.

(Witness excused.)

The Court: Do you have any further evidence for the Petitioner? [241]

Mr. Webster: Yes, your Honor.

The Court: We will be recessed at this time for ten minutes.

(Short recess taken.)

The Court: Proceed.

Mr. Webster: Mr. Tompkins.

Whereupon,

CHARLES B. TOMPKINS

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you tell us your name, please?

The Witness: Charles B. Tompkins.

Direct Examination

By Mr. Webster:

Q. Mr. Tompkins, what is your occupation?

A. I am a certified public accountant.

Q. How long have you been practicing in that capacity? A. About thirty-odd years.

Q. You are admitted to practice here in California? A. Yes, since 1928.

Q. There has been testimony to the effect that you worked for Mr. Aye, is that correct?

A. I did.

(Testimony of Charles B. Tompkins.)

Q. Would you state the dates? [242]

A. Well, approximately the early part of 1942 until about the latter part of 1946.

Q. In the latter part of 1946, as I understand it, Mr. Aye retired; is that right?

A. That is right.

Q. Did you have anything to do with the books and ledger accounts of Wilshire and Western Sandwiches?

A. Yes. Mr. Aye called me into that in about August of 1942. From then on I have had pretty general charge of those books.

Q. Mr. Tompkins, I call your attention to a ledger account appearing under the tab "Liabilities," entitled "Interest Payable Accrued," and I ask you whether you can identify the handwriting.

A. I think everything on that page—yes, everything on that page is my handwriting.

Q. Would you briefly explain to the Court the significance of the entries found on that page?

A. Well, when Mr. Aye was making out the tax return for 1942, the question of interest on the notes advanced by the stockholders came up, and it was found then that no interest had been accrued, so I made that first entry accruing the interest up to the end of December, 1942.

Q. In what amount?

A. That was in the amount of \$1,687.50. [243]

Q. There is a posting reference to J-14; would you—

A. That is the journal entry on which the item

(Testimony of Charles B. Tompkins.)

is set up and charged to the expense account at the bottom of the page.

Q. Can you identify the handwriting?

A. Yes, I wrote it.

Q. Would you read to the Court the contents of that entry?

A. The entry charges \$1,500 to interest expense of 1942, under \$187.50 against the earned surplus, where the interest accrued in 1941 from the time of the notes up to the end of that year, and then the liability is set up as interest payable accrued for \$1,687.50.

Q. Can you remember when you made this entry?

A. I think it must have been along in February, or possibly March, of 1943.

Q. With respect to the first entry on the ledger account entitled "Interest Payable Accrued," when did you make that entry?

A. That was made at the same time. It was dated back to December 31st, because we were closing the books for the year 1942.

Q. Would you kindly describe the succeeding entries in general terms which you find on that page?

A. The next entry was made at the end of March, 1943, [244] and covered the accrual of three months' interest, and after that the entries were made monthly and accrued the interest of the current month clear up to the time the notes were finally paid.

(Testimony of Charles B. Tompkins.)

Q. Can you indicate whether this interest payable accrued account reflects the payment of any interest?

A. Yes. In November of 1943, interest amounting to \$3,055.86 was paid to the noteholders, and again in March of 1945, \$682.10 was paid, and that was all the interest that was paid on those notes.

Q. Mr. Tompkins, I note that the posting reference, with respect to virtually all of the succeeding entries that follow the first entry on the interest payable accrued account, refer to SJ-2. Would you kindly explain the significance of that posting reference?

A. "SJ" was short for standing journal, and the standing journal covered the entries that were made every month, and instead of having to write them each time, just the amounts only were written in columns spread across the page.

Q. Were these standing journal entries in your own handwriting?

A. Some were in my handwriting, and some are in the bookkeeper's handwriting.

Q. Mr. Tompkins, I refer you now to the ledger account page which bears at the top the title "Interest [245] Expense," which appears under the tab "Expenses" in the general ledger of Wilshire and Western. Will you kindly explain briefly to the Court what you find on that page?

A. That was the expense charge for interest that was offset by the liability for the accrual, and each year that was closed off into operating expenses.

(Testimony of Charles B. Tompkins.)

Q. There is a posting reference with respect to the first item appearing on that page to J-14?

A. That entry was for the \$1,500 accrued for the year 1942.

Q. That is the same reference as the—

A. Same reference as the accrual of \$1,687.50 referred to just now, except that only part of it was charged to the current year's expense.

Q. Mr. Tompkins, a question has been raised in the course of this trial with respect to the date upon which the contents of pages 4, 5, and 6 under the tab "Journal" were actually made. I believe you were in court at the time that Mr. Aye testified that those pages were in his own handwriting, is that correct?

A. Yes, that is correct.

Q. J-7 is the page following J-6. Could you recognize the handwriting on that page?

A. That is my handwriting.

Q. The first entry bears what date? [246]

A. June 30, 1942.

Q. Do you recollect making that entry?

A. Yes, I made the entry; it would be sometime later than that.

Q. How much later?

A. That I can't tell you exactly. Probably in the next two or three months, because I didn't go in there until August, so it must have been that much later. [247]

Q. Do you recollect seeing the preceding pages to which I have made reference, J-4, 5 and 6?

A. They have been in the ledger since I saw it.

(Testimony of Charles B. Tompkins.)

Q. Which was in August of 1942?

A. On or thereabouts, yes.

Q. Did you make any use of the correcting entries which are contained in J-4, 5 and 6, when you arrived in August, 1942?

A. Oh, yes, I have embodied them in some working papers of mine where I was trying to bring the books down to date, whatever that date was at the time. I think I tried to get a trial balance as of June the 30th when I made this first entry in my own handwriting.

Q. You employed some of the figures of Mr. Aye?

A. Oh, yes. These all had to be put on to get a new balance sheet as of December the 31st.

Q. I call your attention to the ledger account entitled "Advances by Stockholders", which bears the number 203, and which appears under the tab "Liabilities" in the general ledger of Wilshire and Western. I ask you whether any handwriting on that page is familiar to you.

A. All of it is.

Q. Is any of it yours?

A. Yes. The last three items showing payments of ninety-nine hundred odd, \$10,000 and \$5,000—in other [248] words, the payment of the \$25,000 of notes originally set up is in my handwriting, and I know the handwriting of the previous entry of \$10,000.

Q. Whose writing was that?

A. That was a bookkeeper that stayed there for a short time named Beverly Priest.

(Testimony of Charles B. Tompkins.)

Q. Do you know the person who wrote the preceding two, which would make it the first and second entries appearing on that page?

A. Yes. That is Mr. Aye's handwriting.

Q. At the time that you made your first entry in your own handwriting, which is the date April 30, 1943, were these preceding entries on that page?

A. They were.

Q. At what time did you make the entry which is dated April 30, 1943?

A. Probably sometime in May. It is generally about the latter third of the month before the books are ready to close, so I should guess that it would be somewhere around May the 20th of 1943 that I made that entry.

Q. Mr. Tompkins, would you state whether you are familiar with the cash and accrual method of keeping books?

A. Yes, indeed.

Q. Will you state what method was used in the keeping of these books? [249]

A. Well, both, but largely cash. All sales were made for cash and all bills were paid for each month that could be paid before the books were closed for that month. In other words, the books were kept open until perhaps the 10th or 15th of the following month, and the entries were charged back as of the previous month to get all the payments made, so no accounts payable appear on the books except as between interlocking companies; that is any one of the other three companies that Mr. Carpenter operated might owe Wilshire and Western or be owed by Wilshire and Western.

(Testimony of Charles B. Tompkins.)

Q. How do you explain the significance of the interest payable accrued account?

A. That was one of the accruals that we had to set up because that wasn't paid every month. That was paid when Mr. Carpenter ordered it to be paid.

Q. Do you know on what basis the tax returns of Wilshire and Western were prepared?

A. I believe it is on an accrual basis. I prepared them. They are there.

Q. I show you now the 1942 and 1943 income tax returns of Wilshire and Western, and ask you if you can state upon what method these returns were prepared.

A. Question 10 answers it. It says that the return is made on the basis of accruals.

Q. You are looking now at the 1943? [250]

A. I am looking at the 1943 return, and the 1942 return—the same answer to the same question.

Mr. Webster: That is all, your Honor.

Cross Examination

By Mr. Maiden:

Q. Mr. Tompkins, the entries that you made in the books when you went there in August 1942 were pursuant to instructions from Mr. Aye?

A. I think so, yes.

Q. I believe you stated that you set up interest accrual accounts for 1942, that you actually set them up sometime in 1943?

A. Just as we were closing the books for 1942, yes.

Mr. Maiden: No further questions, if the Court please.

The Court: You are excused. Call your next witness.

(Witness excused.)

Mr. Webster: That is all for the Petitioner, your Honor. However, if your Honor please, at the opening of this case yesterday I made a request for the privilege to make a motion at the end of Petitioner's case with respect to the bringing on of Mr. Odell as a witness. Mr. Odell was the attorney who was active in the formation of Wilshire and Western and is still active in its legal affairs. I [251] stated then that the main purpose for desiring to have Mr. Odell appear was that it was understood some question was raised as to whether there was or was not any back dating on the issuance of notes and of stock, whether there was possibly any back dating of minutes.

Furthermore, an additional point was whether the letter of December 5, 1941, which has been admitted in evidence was in fact prepared and dispatched on that date.

Mr. Odell right now has a 103 fever, and we felt that we might be able to get along without him. However, at this time I should like to ask of government counsel whether he is in a position to state whether any contention with respect to the back dating of the issuance of the notes and of the stock certificates and of the delivery thereof and of the making and execution of signing of the minutes of November 13, 1941, meeting will be subject to attack in brief?

Mr. Maiden: Your Honor, that is an unfair question at this time. I am unable to answer it, and I will not be able to answer it until I read the record.

Mr. Webster: In that case, your Honor, I should like to make the request and motion that Mr. Odell be permitted to testify sometime the latter part of the next week if it fits the Court's calendar. I spoke to Mr. Odell last evening and he told me that his doctor anticipated that [252] Penicillin treatments that he is receiving now will be able to get him better by the end of next week.

Mr. Maiden: I will say this, if the Court please, in order to accommodate the situation, that if Mr. Odell is not able at the end of this calendar to come here and testify, I will agree that the case may be held up for the receipt of his deposition.

The Court: I was going to suggest that very thing, and I not infrequently allow depositions to be taken after the case has been tried to pick up some remnant of the case. We will hear Mr. Odell this next week if we can work it in, unless, of course, if this docket should break as they sometimes do before he is able to come in, why, we will simply have to take a deposition. I don't see how we can set a time, not only on account of his condition, but on account of this docket. I hardly see how we can set a date exactly. Now, I would think that if he wants to take his testimony, and, of course, sometimes an attorney prefers testimony to a deposition—they are never quite the same perhaps—that it would be preferable to get that taken

before the end of Tuesday, but, of course, he may not be in condition to do it by that time. After Tuesday this docket it seems to me, unless there are some breaks in it, it is going to be pretty heavy, and it might cause us to take the deposition instead. We will get the testimony by working it in on this docket or [253] by the deposition.

Mr. Webster: That will be satisfactory.

I should also like to make two motions at the conclusion; one, is to amend 5-A of the petition to conform to the proof.

The Court: In what respect?

Mr. Webster: Your Honor, the petition states that the original plan was to issue \$30,000 of capital stock, and that uncertainty existed at that time as to how much additional would be required in the form of loans. This statement of fact is inaccurate, as has been brought up by the evidence, and I would request permission of the Court to amend the pleadings to conform to the proof.

The Court: Is there any objection?

Mr. Maiden: No objection, if the Court please.

The Court: Very well, you will be permitted within 10 days to file your amendment to Paragraph 5-A in writing. Now, that means that it will have to be written and filed.

Mr. Webster: Yes, your Honor.

Further, I should like to make the motion that Petitioner be permitted to withdraw, I believe, all exhibits with the privilege of substituting photo-stats thereof.

The Court: Well now, counsel, we try these

cases all over the country. We can't leave our records all over [254] the United States and Hawaii, otherwise the taxpayers of this country would be in a rather bad fix to try these cases. If you have particular exhibits that you really need to file a motion, why, you determine which particular exhibits you need to substitute, and then I will consider it, but I am not going to grant a blanket motion to withdraw any exhibits.

Mr. Webster: I can specifically limit myself to the stock book, which I believe we will have use for.

The Court: You will be permitted to withdraw the stock book unless there is some objection.

Is there any objection?

Mr. Maiden: No objection.

The Court: It is not within the control of the opposing party, of course, either way, but sometimes there are exhibits that one of the other parties might not want to substitute because of the authenticity of a signature or something. There being no objection—

Mr. Webster: I am sorry, your Honor. If your Honor please, you have already given permission to withdraw certain of the pages in the general ledger.

The Court: Yes, that has been done. Permission will be given to withdraw the stock book.

The Clerk: That is Exhibit No. 17, if the Court please.

The Court: Exhibit No. 17, and you will be permitted [255] to substitute a photostatic copy.

Now, is the entire stock book in evidence? I mean is it all pertinent, or is it only certain portions?

Mr. Webster: Your Honor, the first eight stubs, I believe, and any certificates which are attached to those stubs are the only portions of the stock book which are in evidence. It is either 8 or 9 stubs, I am not sure which.

The Court: Well, permission is given to substitute the stock book.

Now, this could be attended to just as well before the end of the case, but it might as well be attended to now. A while ago evidence was offered to impeach the testimony of the Witness Carpenter. Objection was made in such terms as I didn't think was a good objection. You simply objected because it wasn't within the issues. No objection was made because there was not then offered a conviction. Then the question went to an indictment. Later it was brought out that he pleaded *nolo contendere* and paid a fine——

Mr. Webster: If your Honor please, may I make this request, that the court room be cleared if we are going into this matter?

The Court: Well, all I am going to say is that instead of sustaining that objection—there will be nothing further stated that will be prejudicial to the minds of anyone—instead of sustaining that objection, I am withdrawing [256] that ruling. I still think it is good, but in the interest of absolute fairness, I am going to withdraw that ruling and withhold my ruling and let you gentlemen brief the question as to whether the facts—and I won't make

any further reference as to what they are—do constitute such as to impeach veracity or credibility. I am inclined to think that probably they do not, but it is rather close.

Mr. Shearer: Will your Honor permit on that a motion to strike in the brief in the event——

The Court: Well, I don't think you need a motion to strike. I will consider that as an effect of credibility or not, as I am convinced by your briefs, withholding my ruling accordingly instead of overruling the objection as I did at that time.

Mr. Shearer: I was thinking of the record, your Honor.

The Court: Very well, for the sake of the looks of the record, if I should decide not to consider it, I will consider a motion to strike in your briefs, yes.

Mr. Shearer: Thank you.

Very well, the Petitioner has rested with the exception announced to the taking of the testimony of another witness, either in person or by deposition.

Mr. Maiden: I have one witness to put on, if the Court please. [257]

The Court: Put on your witness.

Whereupon,

FRED WIGNALL

called as a witness for and on behalf of the Respondent, having been first duly sworn, was examined and testified as follows:

The Clerk: Tell us your name, please.

The Witness: Fred Wignall.

(Testimony of Fred Wignall.)

Direct Examination

By Mr. Maiden:

Q. Mr. Wignall, by whom are you employed?

A. The Collector of Internal Revenue.

Q. In what capacity?

A. Chief of the Income Tax Accounts.

Q. As Chief of the Income Tax Account Section, what are your duties, briefly?

A. I have charge of all the records, income tax returns and claims, bookkeeping, listing of all returns.

Q. Mr. Wignall, have you appeared here at my request? A. Yes, sir.

Q. Did you make a search of your records to determine whether or not your records showed the filing of an amended 1941 income tax return for Wilshire and Western, Inc.? A. Yes, sir.

Q. What do your records show in that respect?

A. The records failed to disclose the filing of any amended return for the Wilshire and Western Sandwich Corporation for the year 1941.

Q. Did you make a search to determine whether or not your records disclosed the filing of any claims for refund with respect to the year 1941?

A. I did, sir.

Q. What do your records disclose?

A. The records show that a claim was filed for the year 1941 on January 18, 1945.

Q. Mr. Wignall, you have charge of recording the filing of income tax returns? A. Yes, sir.

(Testimony of Fred Wignall.)

Q. Just when and how are recordings made in the Collector's office upon the filing of returns?

A. Will you be specific? In what type of returns are you interested?

Q. Well, an amended return, increasing or decreasing the amount of the tax liability shown on the original return.

A. They are both handled differently. An additional tax amended return showing additional tax is received by our office, depending whether there was money on the return or not. It goes to the cashier and is sent down to my section. We list the return. A bill is issued if necessary, and returns are forwarded to the Bureau. [259]

If the return is an amended return showing a decrease in tax liability, it goes into the claims section and there a card record is made of the return. The return is then forwarded to the Bureau with a letter of transmittal to be associated with the original return. I am speaking now of corporation returns.

Q. Have you examined all of the card records in all the sections through which the return would pass to determine whether or not a 1941 amended return was filed by this corporation?

A. Yes, I have. I have checked the records for an addition in tax and for a decrease in tax. I can find no record of either one being filed.

Q. Did you check the cards upon which the filing of the return would be listed if one was filed?

A. I did, sir.

(Testimony of Fred Wignall.)

Q. You found no record?

A. No, I did not.

Mr. Maiden: No further questions.

The Court: Cross examine.

Cross Examination

By Mr. Webster:

Q. Have you ever heard of a taxpayer claiming that he filed an amended return or an original return which you didn't find any record of in your office? [260]

A. Yes, sir.

Mr. Webster: That is all, your Honor.

The Court: Any further questions?

Mr. Maiden: No further questions, your Honor.

By the Court:

Q. I want to get some idea, Mr. Witness, as to how often that happens; that is, directing your thoughts to the last question. I have to consider probabilities on this thing. How often do you lose a filed return or have complaint that one has been filed which you find no record of?

A. I wouldn't be able to accurately answer that question. We have had about——

Q. I don't expect you to answer it accurately, of course. I want you to give me the best idea you can.

A. I don't know how to really answer it, sir.

Q. I appreciate it is a hard question, sir. How many returns go through your office in a year?

A. Approximately 3,000,000.

Q. How many in a year would you find missing

(Testimony of Fred Wignall.)

or returns that are claimed to have been filed and that you have no record of?

A. I really have no way of answering it, because all the inquiries of lost returns don't come to my attention.

Q. How many come to your attention in the course of a year?

A. Well, I would say approximately—and it is an [261] approximation—100.

Q. 100 out of 3,000,000?

A. That is right. That is an approximation, sir.

The Court: That is all I wanted to ask.

Any further questions of this witness?

Mr. Webster: No, your Honor.

Mr. Maiden: No further questions.

The Court: You are excused.

(Witness excused.)

Mr. Maiden: Respondent rests, if the Court please.

The Court: Respondent rests. Does the Petitioner have anything further at this time?

Mr. Webster: No, your Honor.

The Court: Now, in case you gentlemen can't get the testimony, or, we will say that we can't get the testimony of this Witness Odell this next week, then you will be left to take a deposition. That makes it hard to set the time for briefs. I suggest that as soon as you find out whether you are going to offer this testimony in person or find out that you are not, that you contact opposing counsel and see me and then we will set the time for filing briefs

according to how the matter of the other testimony is going to be taken.

Mr. Webster: Very well.

(Whereupon, at 4:30 o'clock p.m., Thursday, December 4, 1947, the hearing in the above-entitled matter was adjourned as above noted.)

[Endorsed]: T.C.U.S. Filed Dec. 19, 1947. [262]

Los Angeles, Dec. 12, 1947

PROCEEDINGS

The Clerk: 10638, Wilshire and Western Sandwiches, Incorporated.

Mr. Crouter: E. C. Crouter responding for respondent in that case, for R. E. Maiden, Jr., attorney of record.

The Clerk: Mr. Webster for petitioner.

The Court: Now, do we have anything in this sandwich case excepting the deposition to take?

Mr. Crouter: Yes, your Honor. I believe Counsel wants to substitute exhibits, which he will explain; and it is agreeable to respondent.

Mr. Webster: If your Honor please, you will recall that certain exhibits were withdrawn for the purpose of making photostats. I have here the photostats of ledger accounts of Wilshire and Western Sandwiches, which have been gone over by Mr. Maiden and by the technical assistant in the technical staff's office. The ledger book itself had been marked Petitioner's Exhibit No. 31, on the inside

of the cover, but no mark was placed on the pages themselves, which here are photostated, and I offer these, I understand, without any objection on the part of Mr. Crouter.

Mr. Crouter: That is correct. No objection by respondent.

Mr. Webster: As petitioner exhibits substituted for the Exhibit No. 31 originally submitted. [265]

The Court: Very well. Mr. Clerk you may substitute the matter referred to in lieu of Exhibit No. 31.

Mr. Webster: If your Honor please, I have a suggestion to offer, that each of these pages be designated by an alphabetical letter following the 31, for convenience in briefs.

The Court: That is an excellent suggestion. We often do that. Will you just take the Exhibit and number the pages themselves A, B and C.

The Clerk: I have marked the first page Exhibit 31, the second page will be 31-A, your Honor.

The Court: 31-A, B and C, just mark them.

Mr. Webster: Now, your Honor, one other exhibit which was withdrawn was a stock book, for the purpose of taking photostats of pages contained therein. It appears that the revenue stamps which were contained in the original stock book had a legend on their face which did not come out in the photostat. I discussed this matter with Mr. Maiden and we agreed that we might place a sheet of paper in front of this exhibit indicating the contents of the legend which was written on the face of the revenue stamps in the stock stuff.

The Court: Very well. I take it that the contents that have been attached is a matter of stipulation?

Mr. Crouter: Yes, that offer is agreeable to respondent. [266]

The Court: What exhibit is that?

Mr. Webster: That is Exhibit 17, if your Honor please.

The Court: This matter will be substituted for Exhibit 17, and you will also indicate the page numbers A, B, C and D on that one, if you have several sheets.

Mr. Webster: If your Honor please, I don't think it is necessary in that particular case, because the certificates are numbered.

The Court: Very well.

Mr. Webster: At the conclusion of the petitioner's case a motion was made to amend the petition to conform to the proof, and I have here one original and four conformed copies of that motion.

The Court: Any objection?

Mr. Crouter: I have been advised of this, but I have not had a chance to read it. If the Court please, there is no objection to making the motion to amend or granting the motion, and respondent would merely like to have a period of say 10 days within which to file an answer if deemed necessary. It may be that none will be necessary.

The Court: The motion is granted and the amendment is filed. Respondent is allowed 15 days from this date within which to file answer, if he wishes.

Mr. Webster: Your Honor, with respect to the testimony [267] of Mr. Odell, I have been in contact with him and found out that it is impossible for him to appear before the Court. He won't be ready for any type of legal work until the latter part of next week, and accordingly, I request that permission be granted to take his deposition for inclusion in the testimony in this case.

Mr. Crouter: That is agreeable to respondent, at a convenient time, of course.

The Court: If that be stipulated by the two of you in accordance with our rule 45(e), I believe it is and duly set forth, I will say now that your application will be granted to take the deposition, and deposition ordered taken prior to January 1, 1948. That is all we have, is it? Except the setting of briefs.

Mr. Webster: Yes, your Honor.

The Court: Very well. Briefs will be simultaneous briefs to be filed by February 1, 1948, reply briefs by February 25, 1948.

The Clerk: The record shows, if your Honor please, that a copy of the motion to amend the petition to conform to the proof is now being served on the parties litigant.

The Court: I believe that disposes of that, doesn't it?

Mr. Webster: Yes, your Honor. Thank you.

(Whereupon at 11:00 o'clock a.m. December 12, 1947, the hearing in the above entitled matter was closed.)

[Endorsed]: T.C.U.S. Filed July 8, 1948. [268]

The Tax Court of the United States

Docket No. 10638

WILSHIRE AND WESTERN SANDWICHES,
INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DEPOSITION OF ROBERT A. ODELL

Deposition of Robert A. Odell, taken on behalf of the Petitioner, at Room 1011, Van Nuys Building, 210 West Seventh Street, Los Angeles, California, on Monday, December 22, 1947, at 4:00 o'clock p.m., before Virginia K. Pickering, a Notary Public within and for the County of Los Angeles and State of California, pursuant to the annexed stipulation to take deposition.

Appearances of counsel: Martin H. Webster, Esq., 320 Bartlett Building, 215 West Seventh Street, Los Angeles, California, appearing on behalf of the Petitioner. Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, of counsel: R. E. Maiden, Jr., Attorneys for Respondent. [271]

ROBERT A. ODELL

called as a witness on behalf of the Petitioner, having been first duly sworn, deposed and testified as follows:

(Deposition of Robert A. Odell.)

Direct Examination

By Mr. Webster:

Q. Would you kindly state your name?

A. Robert A. Odell.

Q. And your occupation?

A. Attorney at law.

Q. How long have you been in the practice of law?

A. I was admitted in June, 1905, and I have been practicing in Los Angeles since January 1, 1906.

Q. What sort of practice have you had?

A. Well, general practice, all phases of the law, without many criminal cases.

Q. Have you heard of Wilshire and Western Sandwiches, Inc.?

A. Yes.

Q. Would you identify them?

A. Well, it is a corporation.

Q. They are your clients?

A. Yes, they have been my clients.

Q. How long have they been your clients?

A. Well, since the incorporation of the company.

Q. Are they your clients now?

A. Well, yes, excepting that I don't want to make [272] any client's disclosures. There has been some change in the ownership, and I may not be their attorney when that is fully effected, but for all purposes, I imagine, connected with this matter, I have been attorney for them. That is, our firm has been, Tanner, Odell & Taft.

(Deposition of Robert A. Odell.)

Q. You say you have been the attorney of Wilshire and Western Sandwiches, Inc., since its incorporation. Were you active in the incorporation of that?

A. I did the legal work in connection with the corporation, application for permit and matters of that sort; such matters as they have conferred with me about.

Q. Mr. Odell, I will show you Petitioner's Exhibit 12 in this matter, being minutes of a meeting bearing date of November 13, 1941. I ask you whether you have seen those minutes before.

A. Yes.

Q. Would you kindly state all you know in connection with those minutes?

A. Well, I prepared these minutes and they are a correct statement of what took place at the meeting on that day, November 13, 1941.

Q. There was a meeting on that date?

A. Yes; 4:00 o'clock in the afternoon.

Q. Would you kindly tell how it is you know there was a meeting on that date?

A. Well, I prepared these minutes, and the minutes [273] recite it took place at that time. My journal entry, kept in the regular course of business, shows a meeting at that time. I recall the attendance at the meeting and the supervision of the holding of the meeting, and seeing to it that these things took place which are recited in the minutes.

Q. Would you describe more fully the manner in which the meeting was held?

(Deposition of Robert A. Odell.)

A. It was held at this room, 307 Transamerica Building, 649 South Olive Street, in Los Angeles, which is the office where Mr. Simon, one of the incorporators, had his office.

Q. Who were in attendance at that meeting?

A. These persons whose names are given in the minutes as having been present at that time.

Q. Would you state who they were?

A. They were Harry B. Carpenter, William H. Simon, Mike Lyman, and M. A. McDonnell. Mr. Jobson signed a consent to the meeting. He was one of the original incorporators, also. I don't think he attended.

Q. Would you kindly state exactly what you did at that time?

A. Well, I had the meeting properly called to order and my recollection is that I read these minutes and had the action taken by the vote of the board for each one of these actions as they show here on the minutes.

Q. Is that your customary procedure or is it an [274] exceptional method of handling a corporate meeting?

A. That is my customary procedure for organization meetings, and any other meeting. If for any reason they don't take the particular action, the minutes are changed before they are signed and put in the minute book.

Q. You have these minutes prepared before the meeting? A. Yes.

Q. What information did you have with respect

(Deposition of Robert A. Odell.)

to the subject matter of this particular meeting at the time that you prepared these minutes which, as you say, was before the meeting?

A. Well, that covers a good deal of territory. Mr. Carpenter advised with me from time to time above the matter involved here, and I had the information from which the minutes were prepared, on which the action was taken, from his statements and conferences with him. I may have conferred with the other gentlemen from time to time, but not to any great extent.

Q. With particular respect to the contents of these minutes, can you recall when you received the information which is set forth in those minutes? A. Well, I can't tell you exactly.

Q. Can you approximate how much before the actual meeting date you learned of the proposed action which was to be taken at that meeting? That is, just an approximate date.

A. Well, referring to our firm journal, I find an [275] entry of October 9th, "Wilshire and Western Sandwiches, Inc., drafting resolution, minutes, etc."

Then, on October 10th—and this is 1941—"Wilshire and Western Sandwiches, Inc., drafting resolutions, minutes, etc. Conference H.B.C." That is Harry B. Carpenter. And a charge to services for reincorporation, permit, lease, and related matters, \$250.00.

So I would say that on those days I was working on the resolutions and the minutes, preparing the

(Deposition of Robert A. Odell.)

matter for this meeting. Now, whether it was fully completed at that time or the draft was in a rough form or what, I have no recollection. But I might explain that I don't want to volunteer things in addition to what is asked me, although I might say this: that our firm has many, many years followed a custom in its business of having the individual members enter on a daybook each day things that occur. We don't always get it all in, but there is a record there of various things, cash transactions, and everything else.

These daybooks are gathered up each morning in our Los Angeles office, and the same thing is done in our Santa Monica office, and the books are gathered up there and duplicates are made of the entries on those books. The Santa Monica office sends its copy here and we send a copy to the Santa Monica office, so we have duplicate records in our Los Angeles and in our Santa Monica offices.

We put down various things that happen. We have found [276] frequently it is helpful as a reminder of what we have done and our charges and all that kind of thing.

These entries I speak of were made in the regular course of business and copied in that way.

Q. Mr. Odell, the minutes with respect to which we have been speaking contain a resolution authorizing the issuance of notes to each of Harry B. Carpenter, M. A. McDonnell, Mike Lyman, and William H. Simon. Can you state whether those notes spoken about in those minutes were ever

(Deposition of Robert A. Odell.)

issued? A. Yes.

Q. When were they issued?

A. Well, they were drafted by me, prepared by me, and they were dated November 13, 1941. They were delivered by December 5, 1941. Now, the reason I say by December 5th is that on December 5, 1941, I wrote to Mr. Carpenter and delivered the certificate of stock to him for 1,000 shares and a promissory note—one of these notes—to him for \$8,333.34. In the letter I state—and I have a copy of it before me—that I have delivered promissory notes of the corporation as follows:

“M. A. McDonnell, \$8,333.33; William H. Simon, \$4,166.67; Mike Lyman, \$4,166.66.”

I wrote to Mr. McDonnell on December 5, 1941, and enclosed Certificate No. 2 for 1,000 shares, and also the promissory note from the corporation to him in that same sun. [277]

I do not find any letter to Mike Lyman or William H. Simon, so I don't know whether I mailed it to them or delivered it to them. I wouldn't think I went over there to deliver it to them, but I just can't recall quite how that was done, whether it was by messenger or somebody picked it up, or what.

Q. In any case, your letter of December 5th, addressed to Mr. Carpenter, by December 5th the notes had been delivered to Mr. Simon and Mr. Lyman. Have you any evidence as to the date when you mailed that letter to Mr. Carpenter, which bears the date December 5, 1941?

A. Well, I find in my file a registry return re-

(Deposition of Robert A. Odell.)

ceipt showing a receipt by Mr. Carpenter 12-6-41. I am quite familiar with Mr. Carpenter's handwriting, and this is his signature. The return card is dated at Glendale December 6, 1941, and the letter to Mr. Carpenter was addressed to him at 625 Cumberland Road, Glendale.

This isn't clipped on the copy of the letter, but it is in my files. I find a memorandum on the letter, "Copy of letter to Mr. Carpenter (registered)." I am quite sure that is the return receipt of that registered letter with the stock and the note.

Mr. Maiden: It is stipulated by Respondent that his counsel has read the return receipt of a registered letter and that the contents of this receipt are as just testified to by Mr. Odell. [278]

Q. (By Mr. Webster): Mr. Odell, again referring to the November 13, 1941, minutes, they contain a resolution dealing with the issuance of shares of stock to the same four individuals about whom we have been speaking and to whom you have testified notes were delivered. Were such share certificates issued? A. Yes.

Q. In what amounts?

A. Well, you have the certificate book there?

Q. I show you Petitioner's Exhibit No. 17, which has been identified as the stock ledger book of Wilshire and Western Sandwiches, Inc.

A. I am familiar with that. The writing on these stubs, except as to the receipt for the stock, is in my handwriting, and I filled out the stock certificates and filled out the stubs.

(Deposition of Robert A. Odell.)

Q. When were those stock certificates issued?

A. Well, they were dated November 13, 1941, and that is my best recollection. The canceled stock certificates in here, which were issued at that time, bear the same date.

Q. You are referring to Certificates Nos. 3 and 4?

A. Nos. 3 and 4. Those were surrendered in order that some small block of stock could be issued to Mr. Lardemer.

Q. There is a reference in your letter of December 5, 1941, addressed to Mr. Carpenter, as to the delivery of stock [279] certificates. Are these the stock certificates to which that letter refers?

A. Well, the stock certificates of which these are stubs—in other words, the original stock certificates to Carpenter and McDonnell are not here, but the stubs are.

Q. What I meant was, your letter of December 5, 1941, which you were talking about a few moments ago, I believe makes reference to delivery of stock certificates. A. Yes.

Q. Are these the stock certificates, that is, is this the stock ledger book for the certificates with respect to which that December 5th letter was referring?

A. It is the book of stock certificates, and my letter had reference to the original certificates which were issued from this book, and as to which there is a stub entry on this book.

Q. Would you, therefore, state the dates on which these stock certificates were delivered?

(Deposition of Robert A. Odell.)

A. Well, they were delivered on the 5th of December, 1941, as to Mr. Carpenter and Mr. McDonnell. As I said before, I am not certain just when they were delivered to Mr. Simon and Mr. Lyman, but it was on or shortly before the date; certainly, between November 13, 1941, and December 5th.

I note that Mr. McDonnell signed a receipt for his and that receipt is dated the 5th of December. It is signed for Mr. McDonnell by Mr. Jobson. Mr. Jobson was in Mr. [280] McDonnell's employ. These other dates of the receipt, on the bottom of the stubs, don't seem to be filled in; sometimes we are careless about that.

Q. Calling attention to the revenue stamps which are placed on the stubs of these certificates, do you know when those stamps were attached?

A. Well, they were bought on December 3, 1941.

Q. As a source of information, do you have any information on that, Mr. Odell?

A. I have an entry in this firm journal under date of December 3, 1941, "Wilshire and Western Sandwiches, Inc. Charge. Paid revenue stamps, \$33.60."

I also have a memorandum here from the Wilshire and Western files dated 11-27-41, signed by R.A.O.—that is me—to E.S.—that is Mr. Shilling, an attorney in our employ—in which I requested him to get these revenue stamps and specified the denominations. That is dated 11-19-41. It bears the stamp of the post office, "Los Angeles, California, Metropolitan Station. December 3, 1941."

(Deposition of Robert A. Odell.)

Mr. Webster: Off the record.

(Discussion off the record.)

Mr. Webster: On the record.

Mr. Maiden: Referring to the office memorandum record dated 11-27-41, about which Mr. Odell has just testified, Respondent hereby stipulates that the contents of said memorandum [281] are as testified by Mr. Odell.

The Witness: To answer a little further, the denominations here which I asked Mr. Shilling to get, two tens, two ones, twenty-five cents, it looks like, and two fifty cents: that corresponds exactly with the revenue stamps on these stubs. Now, whether they were canceled later or not—they must have been canceled later. That looks like my writing. It may have been Mr. Bassett's, who came in here checking over the books at a later time in 1946.

Q. (By Mr. Webster): Who was Mr. Bassett?

A. He was connected with the Internal Revenue Department. "George L. Bassett, D. C."—whatever that means

Q. He was, in any case, an official of the Collector's office that checked over these stamps, is that correct?

A. That is right. Somebody comes in periodicaly from the Internal Revenue office and will say, "Let's see the books of such and such corporation."

I say, "Here they are," and he goes through them.

It very well may be I put those on and didn't

(Deposition of Robert A. Odell.)

cancel them at the time. They were charged and paid for on that date. By the ledger account of our firm it shows the stamps were paid for in that amount, as shown by that book. This is a copy of the statement I rendered to Wilshire and Western Sandwiches, December 4, 1941, showing the payment of those revenue stamps.

Q. Mr. Odell, you have been testifying with respect to [282] four notes dated November 13, 1941, issued, respectively, to Mr. Simon, Mr. Lyman, Mr. Carpenter, and Mr. McDonnell. Were there any other notes issued to any or all of these individuals by Wilshire and Western Sandwiches, Inc.?

A. Any other notes? I don't recall any at this moment.

Q. In any case, were there ever any notes issued prior to November 13, 1941, or thereabouts, to these four individuals.

A. Well, I don't think so. I don't recall any others. I prepared these, originals of these notes, of which I have a copy.

Q. And you know of no others? A. No.

Q. Mr. Odell, you have been testifying with respect to the issuance of certain shares of stock to these four individuals and also certain shares to Lardemer. Were there any other share certificates issued by Wilshire and Western Sandwiches, Inc., than those which you have been speaking about?

A. None of which I have any knowledge. There were two stock certificates issued—whatever is shown here by the separate stubs—being a reissue out of the Simon-Lyman stock.

(Deposition of Robert A. Odell.)

Q. In the course of your professional practice have you ever had occasion to back-date any document more than one [283] or two days after the particular event?

A. No, I don't back-date documents.

Mr. Webster: Thank you, Mr. Odell. That is all.

Cross Examination

By Mr. Maiden:

Q. Mr. Odell, have you handled the tax matters and did you handle the tax matters of Wilshire and Western Sandwiches, Inc., from its organization through the years 1942 and 1943?

A. No, I didn't handle any tax matters whatever for them.

Q. Do you do any federal income tax work at all, Mr. Odell?

A. Well, to a certain extent, that is, in connection with estates, making fiduciary returns, and sometimes for our clients. We don't like to do it, but it sometimes happens a client will wish you to do it, so we go through it. But we don't desire to, and many times in estates, if they are at all complicated, we have an outside tax accountant do that.

Q. Mr. Odell, do you recall whether or not Mr. Carpenter or Mr. Simon or Mr. Lyman or Mr. McDonnell discussed with you at any time during 1941 and prior to the issuance of the notes and stock certificates, which you have testified about, why it was that the stockholders were proposing to take a part of their advancement to the [284] cor-

(Deposition of Robert A. Odell.)

poration required to build its drive-in and equip it for business, in notes instead of all in stock?

A. I don't think they knew how much it was going to cost. Certainly, as it afterward developed, it cost a great deal more than was originally contemplated. Mr. Carpenter discussed the matter with me, with respect to subscribing so much for stock, and then borrowing what they needed to complete the building from the individual stockholders. But the purpose or the purport of it was not particularly discussed. That is, I don't recall the discussion about that. I am sure I never had any discussion with any of the other gentlemen at all about the matter, except when we had the meeting and authorized the issuance of the notes. You see, Mr. Carpenter was doing the discussing with me.

Q. Mr. Odell, do you recall whether or not it was the intention of the incorporators and eventual stockholders of this corporation that they would purchase from the corporation sufficient shares of its stock with which to furnish the money required to build the drive-in and equip it for business?

A. No, I think they—well, I don't want to guess at things and say what I think. I want to answer your question.

Q. Before answering that question, Mr. Odell, I might refresh your recollection with Exhibit 4-D to the stipulation of the parties in the case, which is a copy of a petition filed with the Corporation Commissioner for permission [285] to issue shares of stock.

(Deposition of Robert A. Odell.)

I call your attention to a provision appearing on page 4 of this exhibit, to the effect that "It is proposed also to sell additional of its stock for cash to the incorporators, if it should become necessary to do so, for the purpose of completing the building or equipment or for further expanding the business or facilities thereof."

Does that refresh your recollection any on the point?

A. This petition states, in the first part of that paragraph, that "It is proposed to sell and issue at this time 1,500 shares of the stock for that purpose, and to pay the expenses of incorporation and to borrow from the individual stockholders or incorporators additional money sufficient to complete the building and equipment."

And this last statement, "It is proposed also to sell additional of its stock for cash . . . should it become necessary . . . for the purpose of completing the building": now, not to be argumentative at all, but it is my recollection that they didn't know just how much it was going to cost. They thought it would be somewhere around \$30,000; to use this \$15,000 worth of stock issued, and borrow money, if necessary.

Experience has shown, a lot of these drive-ins have cost a good deal more than was originally contemplated.

So that the statement should also be made, they might not have made those individual loans or made the borrowings, [286] but they wanted to be

(Deposition of Robert A. Odell.)

in a position to issue additional stock to the original stockholders if they desired so to do. The prayer of the petition was for the issuance of all the stock to them for cash, notwithstanding it had also said \$15,000 at that time. My recollection is that the permit was made to issue them the whole seventy-five thousand, which, of course, didn't mean they had to take it.

Q. Now, Mr. Odell, this stipulation of the parties discloses that either some or all of the stockholders in the petitioner in this case likewise organized and became stockholders in various other drive-in restaurants of the type operated by this petitioner, and that in each one of these cases stock and documents, denominated notes, were issued to cover the advances made for the construction of the buildings and equipment. Do you recall whether or not you likewise handled the incorporation arrangements in those other corporations?

A. Well, the only one I had to do with was the Sunset Sandwiches, and the other corporation where they—I have forgotten just who all were in that; there was a different personnel there.

Q. The stipulation will show that, I believe.

A. Yes. The Scrivners, Hulsmans, McDonnell, Carpenter, Lyman and Simon.

Q. That is the only other corporation for this group of men that you prepared the corporation records and minutes [287] and issuance of stock and notes, and so forth?

A. That is right. There was one, Manveda, Inc.,

(Deposition of Robert A. Odell.)

which has since been dissolved. I don't think it was of the same structure.

Q. But, Mr. Odell, I believe that you have testified that the purpose these stockholders had in mind in this particular case, in taking part of their advancement in the form of loans, was not discussed with you.

A. I don't know what you mean, "taking advancement in the shape of loans."

Q. I might call your attention to the fact, Mr. Odell, that in the stipulation it is stipulated that, beginning in May 1941, and ending on November 19, 1941, the stockholders in this corporation had advanced to the corporation the sum of \$55,000.

Now, it has further been developed in the case that stock was not issued for that entire amount of money advanced, but that part of the advancement, total advancement, was taken in the form of promissory notes issued to the stockholders.

Now then, I want to know whether or not these stockholders advised you why it was that they wanted to take part of the advancement in notes, rather than taking it all as stock.

A. Well, I don't know about the \$55,000. The original plan, as shown by, or, at any rate, developed at [288] the time the application was made to the Corporation Commissioner, it was rather plain that the stock which they proposed to actually buy at that time was \$15,000. I don't recall, but I rather think the building proceedings were going on during the summer and up to the time when

(Deposition of Robert A. Odell.)

this action was taken on November 13th. The \$15,000 in stock evidently increased to \$30,000 by that time, and the advancements made amounted to this other sum, \$25,000.

There had been a rather general understanding, as I got it from Mr. Carpenter, that they would buy some stock and make individual loans from the incorporators to carry on the building, but they weren't obliged to.

Q. I am not asking you that. Of course, that is a matter of law. But the point I am trying to clear up in the record is whether or not these stockholders, after the building had been completed, the money had been advanced, that they preferred to take part of their advancement in the form of notes rather than entirely as stock.

A. Not at that time. I think that was the idea right along. What was contemplated was, they would buy stock and they would also make loans.

Q. Did they tell you why they did not want to put up the entire amount of money required in the form of stock purchases?

A. No, that wasn't discussed, that I recall, to any extent. I don't remember discussion about it, excepting they [289] didn't know what the building was going to cost, and they — when I say "they", please understand I mean only Mr. Carpenter, who had talked to me about the matter. I didn't talk to these other gentlemen about it in the formative stages. I assumed he spoke for them. And when I held the meetings, what took place,

(Deposition of Robert A. Odell.)

of course, was actually as shown by the minutes. I didn't go into detail talking with all these other gentlemen about any of these things, except when we held the meetings.

Q. Mr. Odell, I don't mean to be impertinent or to in anywise impinge your absolute integrity, but Mr. Carpenter testified in this case that notwithstanding the fact that he had signed the affidavit attached to the petition to the Corporation Commissioner, which affidavit of course states that he had read and understood the contents of that application, that he, in fact, didn't read it and didn't know its contents. Do you recall whether or not you presented this application to Mr. Carpenter to be read by him and notarized?

A. This is a copy of the certified original. He signed it and swore to it before me on that day. That is what happened. I don't know what Mr. Carpenter testified to. I didn't talk to him about his testimony.

Mr. Maiden: Well, you can rely upon my statement he did testify to that, in substance. I think Mr. Webster will agree. I believe that is all. [290

Redirect Examination

By Mr. Webster:

Q. Mr. Odell, is Mr. Carpenter a client of your firm? A. Yes.

Q. How long has he been a client of your firm, approximately?

A. Oh, about 35 years ago. By that I mean that over that period of time, from time to time, he

(Deposition of Robert A. Odell.)

has employed us and we have represented him in legal matters, for places he has been interested in. That doesn't mean that he doesn't have other attorneys at times. I don't know what other attorneys he may have.

Q. You are a senior partner in this firm of Tanner, Odell & Taft?

A. Well, I don't want to emphasize the senior part of it. Mr. S. W. Odell, my uncle, is my senior in years in the firm. But Mr. Donald Odell is my cousin and junior in years. Mr. Taft is my junior in years.

Q. How many do you have in this firm, Mr. Odell?

A. Well, we have four now. Judge Taft and Judge Tanner passed away; Mr. Shilling is associated with us.

Mr. Webster: That is all.

/s/ ROBERT A. ODELL.

Subscribed and sworn to before me this 15th day of January, 1948.

/s/ VIRGINIA K. PICKERING,

Notary Public in and for the County of Los Angeles, California.

My Commission expires May 10, 1951. [291]

To the Tax Court of the United States:

I, Virginia K. Pickering, the person named in the attached stipulation to take deposition, hereby certify:

(Deposition of Robert A. Odell.)

1. That I proceeded on the 22nd day of December, A. D. 1947, at the offices of Tanner, Odell & Taft, 1011 Van Nuys Building, 210 West 7th Street, in the City of Los Angeles, State of California, at 4:00 o'clock p.m., under the said stipulation to take deposition, and in the presence of Martin H. Webster and R. E. Maiden, Jr., the counsel of the respective parties, to take the following deposition, viz:

Robert A. Odell, a witness produced on behalf of the Petitioner.

2. That the witness was examined under oath at such times and places as conditions of adjournment required, and that the testimony of the witness was taken stenographically and reduced to typewriting by me or under my direction.

3. That after the testimony of the witness had been reduced to writing the transcript of that testimony was read and signed by the witness in my presence and that the witness acknowledged before me that his testimony was in all respects truly and correctly transcribed.

4. That, after the signing of the deposition in my presence, no alterations or changes were made therein.

5. That I have no office connection or business employment with the Petitioner or its attorney.

/s/ VIRGINIA K. PICKERING,
Notary Public in and for the County of Los Angeles, State of California. [292]

My commission expires May 10, 1951.

[Title of Tax Court and Cause.]

STIPULATION TO TAKE DEPOSITION

It Is Hereby Stipulated and Agreed by and between the parties to the above entitled action, through their respective counsel, that the testimony of Robert A. Odell witness on the part of Petitioner in said action, may be taken pursuant to Rule 45 of the Rules of Practice before the Tax Court of the United States, before Virginia K. Pickering, Notary Public in and for Los Angeles County, California, on Monday, the 22nd day of December, 1947, at 1011 Van Nuys Building, in the City and County of Los Angeles, California, at 4:00 o'clock in the afternoon of said day, and if said deposition is not completed on said day, it may be continued from day to day thereafter until same is completed.

It Is Further Stipulated and Agreed that the testimony may be written down in shorthand writing by a shorthand reporter and thereafter transcribed into writing and shall then be read to or by the said witness, corrected, subscribed and sworn to by said witness; that the said deposition and testimony, when so taken, may be read and used in evidence in said cause by either party on any trial of said action or proceeding therein, subject to the same objections and exceptions as if said witness were personally present on the witness stand, but without objection or exception to the time, place

or manner of taking the same, or the form of the question, unless noted at the time.

Dated this 22nd day of December, 1947.

/s/ MARTIN H. WEBSTER,
Attorney for Petitioner.

/s/ R. E. MAIDEN, JR.,
Attorney for Respondent.

General Reporting Company, 215 West 5th
Street, Los Angeles, Calif. MIchigan 4341. [293]

[Title of Tax Court and Cause.]

STIPULATION

It is hereby stipulated by and between Wilshire and Western Sandwiches, Inc., Petitioner, and the Commissioner of Internal Revenue. Respondent, by their respective counsel, that the following facts shall be taken as true; provided, however, that this stipulation shall be without prejudice to the right of either party to object at the hearing to any part thereof on the grounds of immateriality, or to introduce other and further evidence not at variance with the facts herein stipulated;

1. The tax years involved are the calendar years 1942 and 1943.

2. The Petitioner is a corporation organized under the laws of California with its principal place of business at 3180 West Sixth Street, Los Angeles, California. It filed its returns for the tax years involved with the Collector for the Sixth

District of California. The Petitioner kept its books and prepared its returns on the accrual basis.

3. The Petitioner was incorporated March 24, 1941 with an authorized capital stock of 7500 shares of common stock of the [284] par value of Ten Dollars (\$10.00) per share. Petitioner was formed for the purpose of engaging in the drive-in restaurant business. In addition to other powers granted to it in its Articles of Incorporation, Article XII empowers the corporation to borrow money and issue its notes therefor.

4. On April 26, 1941, a lease was entered into between Robert Ashley Pettey and Julia Faye Pettey, lessors and Wm. H. Simon, lessee. A copy of the provisions of the lease which are deemed relevant is attached hereto as Exhibit No. 1-A to this Stipulation.

5. On May 2, 1941, a Supplement to Lease was executed between the same parties who executed the lease dated April 26, 1941. A copy of this supplement is attached hereto as Exhibit No. 2-B.

6. Commencing May 17, 1941, payments were made to the Petitioner by the following individuals and in the following amounts:

Date	Advanced by	Amount
5/17/41	M. A. McDonnell	\$ 3,333.33
6/ 9/41	Wm. H. Simon and Mike Lyman (half each)	3,333.33
6/ 9/41	Harry B. Carpenter	3,333.34
8/22/41	Wm. H. Simon and Mike Lyman (half each)	5,000.00
9/12/41	M. A. McDonnell and Harry Carpenter (half each)	10,000.00

10/30/41	Wm. H. Simon and Mike Lyman (half each)	5,000.00
Date	Advanced by	Amount
10/30/41	Harry B. Carpenter	5,000.00
11/13/41	Wm. H. Simon and Mike Lyman (half each)	5,000.00
11/13/41	Harry B. Carpenter	5,000.00
11/19/41	M. A. McDonnell	10,000.00

The total of all payments from the four individuals above named was Fifty-Five Thousand Dollars (\$55,000) divided as follows:

Name	Amount
Harry B. Carpenter.....	\$18,333.33
M. A. McDonnell.....	18,333.33
Wm. H. Simon.....	9,166.67
Mike Lyman	9,166.66

7. The monies paid as outlined in Paragraph 6 hereof were first used by the Petitioner to defray expenses for preparation of plans and specifications for the erection of a building on the leased premises. Said monies were thereafter used to pay for the construction of the drive-in building and the equipment thereof. A summary of the total amounts so expended, per the books, broken down by months and allocated between building and equipment is set forth below: [296]

	Building	Equipment	Total to Date
1941			
June	\$ 750.00	\$ 750.00	\$ 1,500.00
July	1,011.08	545.00	3,056.08
August	7,129.53	521.02	10,706.63
September	8,864.55	2,272.75	21,843.93
October	5,926.95	1,098.02	28,868.90

			Total to Date
1941	Building	Equipment	
November	3,828.17	1,373.20	34,070.27
December	8,005.77	8,955.79	51,031.83
Add: Prepaid Expenses per Journal Entry Page 6	2,598.63	2,000.00	55,630.46
Total—1941	\$38,114.68	\$17,515.78	\$55,630.46
1942			
January	\$ 2,375.00	\$ 123.60	\$58,129.06
February .....	.....	7,663.66	65,792.72
Totals	\$40,489.68	\$25,303.04	\$65,792.72

8. On or about June 15, 1941, the architect for the proposed building of the Petitioner, Joseph L. Feil, solicited bids for the construction of said building. Four bids were received as follows: [297]

Bidder	Minimum Amount	Date of Bid
Lynch Cannon Construction Co.....	\$21,000.00	6/20/41
Nowell M. Calhoun	19,327.00	6/20/41
Hastings-Quinn, Inc.	18,875.00	6/21/41
Frank A. Woodyard	18,222.00	6/20/41

On July 10, 1941, a building construction contract was entered into between the Petitioner and Frank A. Woodyard under which Frank A. Woodyard agreed to construct a drive-in building and adjacent service building for the sum of Twenty-Two Thousand Six Hundred Fifty-one Dollars (\$22,651.00). Frank A. Woodyard commenced erection of the drive-in building on or about July 25, 1941. By on or about October 25, 1941, the work of Frank A. Woodyard had been substantially completed.

9. On July 14, 1941, the board of directors of the Petitioner held its first meeting. A copy of

the minutes of said meeting are attached hereto as Exhibit No. 3-C.

10. On July 14, 1941, the President and Secretary of the Petitioner applied to the Commissioner of Corporations of the State of California for a permit to issue shares of its stock as set forth in the application, a copy of which is attached hereto as Exhibit No. 4-D. On July 17, 1941, a permit was issued by the Corporation Commissioner of the State of California authorizing the issuance of 7500 shares at par for cash, all in accordance [298] with said permit, a copy of which is attached hereto as Exhibit No. 5-E.

11. On July 14, 1941, Wm. H. Simon, lessee under the lease hereinabove described in Exhibit No. 1-A, duly assigned to the Petitioner as assignee said lease and the supplement thereto dated May 2, 1941, hereinabove described in Exhibit No. 2-B. Consent to said assignment was duly obtained on August 14, 1941. A copy of said assignment is attached hereto as Exhibit No. 6-F.

12. On August 22, 1941, a lease was entered into between Edna R. Vogel, lessor, and the Petitioner, lessee, covering premises adjacent to the property theretofore assigned to the Petitioner by Wm. H. Simon as original lessee and on which the drive-in restaurant was constructed. Said premises were to be used for parking purposes. A copy of said Vogel lease is attached hereto as Exhibit No. 7-G.

13. On or about November 15, 1941, the Petitioner commenced doing business as a drive-in restaurant.

The bank balance of the Petitioner on February 1, 1942 was One Thousand One Hundred Twenty-Six Dollars and Ninety-Eight Cents (\$1,126.98).

14. On the following dates, checks of the Petitioner were issued and delivered to the following named persons in the amounts indicated, with an explanation in the voucher portion of each check as follows: [299]

Name	Date	Amount	Explanation on Voucher
Harry B. Carpenter	4/21/43	\$3,333.34	"Payment on Note"
M. A. McDonnell		3,333.33	"Payment on Note"
Wm. H. Simon		1,666.16	"Payment on Note"
Mike Lyman		1,666.16	"Payment on Note"
Harry B. Carpenter	5/23/44	3,333.33	"Note Acct."
M. A. McDonnell		3,333.34	"Note Acct."
Wm. H. Simon		1,667.17	"Note Acct."
Mike Lyman		1,667.17	"Note Acct."
Harry B. Carpenter	3/23/45	1,666.66	"Bal. on Note"
M. A. McDonnell		1,666.66	"Bal. on Note"
Wm. H. Simon		833.34	"Bal. on Note"
Mike Lyman		833.34	"Bal. on Note"

15. There are attached hereto as Exhibit Nos. 8-H, 9-I and 10-J, respectively, Corporation Income and Declared Value Excess-Profits Tax Returns filed by the Petitioner for the calendar years 1941, 1942 and 1943.

16. The stockholders of Petitioner, or some of them, have entered into similar transactions wherein they advanced [300] money to other corporations for a portion of which they received capital stock thereof and for the balance of which they received documents designated "Promissory Notes". A list of such similar transactions is set out below:

Name of Corp.	Date of Incorporation	Date Com- menced Business	Capital Structure	Stockholders and Lenders
F & LB Corp.	1/17/41	10/ 1/41	\$36,000.00 stock 54,000.00 notes	M. A. McDonnell, B. W. Hulsman, Al Simon, Mike Lyman, Wm. H. Simon, H. Carpenter, L. J. Evans
M & S Foods Inc.	12/28/40	7/ 1/42	\$36,000.00 stock 108,000.00 notes	B. W. Hulsman, M. A. McDonnell, Al Simon, Mike Lyman, Wm. H. Simon, L. J. Evans, H. L. Schrivener, Dorothy Marcus Lyman
Carsim, Inc.	10/ 1/37	6/ 1/39	\$30,000.00 stock 7,500.00 notes	Wm. H. Simon, Mike Lyman, Albert Simon, H. Carpenter, Hallie McDonnell, Ben Hulsman
Simon's Florat, Inc.	2/ 6/41	11/—/41	\$10,000.00 stock 38,097.09 notes	Wm. H. Simon, Mike Lyman, M. A. McDon- nell, H. Carpenter, J. Lardemer
Simon's Beverly Inc.	6/10/40	2/—/41	\$ 9,900.00 stock 29,348.78 notes	Wm. H. Simon, M. A. McDonnell, L. J. Evans, J. A. Lardemer, Al Simon, B. W. Hulsman, Mildred Evans, Mike Lyman
Simon's Five Points, Inc.	2/ 3/41	11/ 1/41	\$10,000.00 stock 41,782.30 notes	Wm. H. Simon, Mike Lyman, J. Lardemer, H. Carpenter, M. A. McDonnell
Simon's Wash- ington, Inc.	1/ 7/41	9/23/41	\$10,000.00 stock 9,498.08 notes	Wm. H. Simon, Mike Lyman, M. A. McDon- nell, J. Lardemer, E. J. Aye
Sunset Sand- wiches, Inc.	8/16/40	1/29/41	\$18,000.00 stock 16,000.00 notes	H. L. Schrivener, C. W. Scrivener, B. W. Huls- man, M. A. McDonnell, H. B. Carpenter, Wm. H. Simon, Mike Lyman
Carleton's Inc.	3/24/37	1937	\$ 7,000.00 stock 2,000.00 notes	M. A. McDonnell, B. W. Hulsman, Ben Carle- ton

In two of the above listed corporations, the notes were not in proportion to the investments made for capital stock. Details are as follows: [302]

Name	Percent of Notes	Percent of Stock
Sunset Sandwiches, Inc.		
H. L. Scrivener	25	16.67
C. W. Scrivener	25	16.67
H. B. Carpenter	25	16.67
H. B. Carpenter, Jr. ....	....	16.67
M. A. McDonnell	8.33	11.11
B. W. Hulsman	8.33	11.11
Wm. H. Simon	4.17	5.55
Mike Lyman	4.17	5.55
Carleton's, Inc.		
M. A. McDonnell	50	26.07
B. W. Hulsman	50	26.07
B. Carleton .....	....	47.85

In all other of the above listed corporations, the notes were in proportion to stockholdings.

17. In all of the above corporations, with the exception of Carleton's, Inc., the Commissioner of Internal Revenue has refused to recognize the documents designated promissory notes as bona fide loans of money by the stockholders to the corporations, but has treated the amounts represented by the notes as investments in the businesses. Appeals are now pending before this Court from the afore-said action of the Commissioner in Simon's Florat, Inc., Docket No. 15309; Simon's Five Points, Inc., Docket No. 15305; Simon's [303] Washington, Inc., Docket No. 15306; Simon's Beverly, Inc., Docket No. 15308; Carsim's, Inc., Docket No. 15307; and Sunset Sandwiches, Inc., Docket No. 10637. In F & LB Corporation and M & S Foods, Inc., 30 day letters have been issued, and 90 day letters will soon be issued.

18. Nothing in paragraph 16 above should be construed as an admission on the part of respondent that the documents designated promissory notes were in fact loans to the corporations, it being respondent's contention as aforesaid that the amounts represented by said notes are in fact investments in the businesses.

/s/ MARTIN H. WEBSTER,
Counsel for Petitioner.

/s/ CHARLES OLIPHANT,
Chief, Counsel, Bureau of Internal Revenue, Counsel for Respondent. [304]

EXHIBIT No. 1-A

LEASE

This lease, made and entered into this 26th day of April, 1941, by and between Robert Ashley Pettey and Julia Fay Pettey, Trustees of the Estate of Mary Emma Pettey, Deceased, hereinafter called lessors; and William H. Simon, hereinafter called lessee;

Witnesseth:

That, in consideration of the payment of rents and performance of the other covenants and agreements herein provided to be kept and performed by the lessee, and on condition that the rents herein provided shall be paid when due, and that each and all of the covenants and agreements herein provided shall be duly and fully performed by the lessee, the lessors have leased, demised, and let, and

Exhibit No. 1-A—(Continued)

by these presents do lease, demise, and let, unto the lessee those certain premises situated in the City of Los Angeles, County of Los Angeles, State of California, more particularly described as follows:

Lots 1 and 2 in Block H of Westminster Place, as per map thereof recorded in the office of the County Recorder of the County of Los Angeles, State of California, in Book 9, Page 61 of Maps;

together with all the rights, easements, and appurtenances to the real property belonging and appertaining and usually had and enjoyed therewith; and all upon and subject, however, to the terms, conditions, exceptions, reservations, restrictions, and provisions herein contained or mentioned;

To have and to hold the same unto the lessee for the term herein specified, and upon the terms, conditions, provisions, and covenants, and subject thereto as in this entire lease set forth, contained, and mentioned. [305]

Lessors hereby represent and warrant that they are the legal owners of said real property herein demised. Lessors further covenant with lessee that the herein-demised land is not zoned or restricted against the uses for which the said land is hereby demised, and lessors further covenant with the lessee that the said demised premises may be used by the lessee for the purposes herein set forth.

Exhibit No. 1-A—(Continued)

I.

TERM

The term of this lease shall be for a period of fifteen (15) years, commencing on the 30th day of April, 1941, and ending on the 29th day of April, 1956.

II.

CONSTRUCTION OF BUILDING

It is hereby agreed, by and between lessors and lessee, that upon the delivery of possession of the above-demised premises to lessee as hereinbefore provided, lessee shall commence the preparation of plans and specifications for the said proposed restaurant building, and thereafter diligently prosecute the work of constructing said building so that a late-model drive-in restaurant building will be erected on the demised premises within approximately 120 days after possession of said premises has been delivered to lessee. The plans and specifications for said building shall be approved in writing by both lessors and lessee, and may, at the option of lessee, provide for the erection of a cocktail bar.

The lessee shall bear the entire cost of constructing said building and equipping and furnishing the same. The said total cost of the entire work of improvement, including the [306] equipment and fixtures installed in said building, shall be not less than \$30,000.00.

Exhibit No. 1-A—(Continued)

The time within which it is contemplated that the drive-in restaurant building will be erected, to-wit, 120 days, shall be extended or such period of delay as may be caused by strikes, lockouts, acts of God, or other conditions beyond the control of lessee.

III.

RENTAL

(a) Lessee agrees to pay as rental for said demised premises during the entire period of this lease an amount equal to six per cent (6%) of the total gross sales made in connection with the business conducted in, on, or from the demised premises as hereinafter more particularly defined, which said payments shall be hereinafter referred to as "percentage rental"; provided, however, that lessee agrees (subject to the abatement provision hereinafter contained) that said rental shall not be less than Seven Hundred Dollars (\$700.00) each month during the term of this lease. Said minimum monthly rental payments of Seven Hundred Dollars (\$700.00) per month are hereinafter referred to as "guaranteed minimum monthly rentals".

In addition to said guaranteed minimum monthly rentals lessee agrees to pay the amount of taxes and assessments hereinafter referred to and provided for in articles XV and XVI hereof.

(b) Said guaranteed minimum monthly rental of Seven Hundred Dollars (\$700.00) each month shall be payable monthly in advance on the first

Exhibit No. 1-A—(Continued)

day of each and every calendar month of the term of this lease after the end of the abatement period hereinafter provided for; provided, however, that, in [307] the event the day for the commencement of said guaranteed minimum monthly rental shall be a day other than the first day of a calendar month, then the first installment of guaranteed minimum monthly rental shall be equal in amount to that portion of Seven Hundred Dollars (\$700.00) as the number of remaining days in said month bears to the total number of days in said month, and thereafter the full guaranteed minimum monthly rental installments shall be paid on the first day of each calendar month of the remainder of the term of said lease.

In addition to guaranteed minimum monthly rentals, lessee hereby covenants and agrees to pay as rental, in the manner provided for in Article XIV hereof, the amount by which the percentage rental exceeds the guaranteed minimum monthly rental required to be paid hereunder. The percentage rental shall be computed monthly, and payment of the excess over the minimum guaranty shall be made in the manner provided for hereinafter in Article XVI.

IV.

GROSS SALES

The term "gross sales" as used herein shall mean and include the full value received by lessee, and by any assignee, sub-lessee, or licensee of lessee,

Exhibit No. 1-A—(Continued)

from all transactions, including all sales, trades, exchanges, and transfers of merchandise of any kind, made upon or from the demised premises or in connection with any business carried on upon the demised premises, whether such merchandise be prepared or consumed upon the demised premises or otherwise, and whether such transactions be at wholesale or retail or for cash or on credit, and in case of sales made on credit, whether payment therefor is actually made or not. [308]

The term "gross sales" shall include all the net revenue received by lessee from sales or transactions from all vending machines upon the demised premises which are not owned by lessee, and all the gross revenue from all vending machines upon the demised premises which are owned by lessee.

The term "gross sales" shall include the value received from all such transactions as aforesaid which result from orders or offers received in connection with the business carried on upon the demised premises, regardless of where such orders or offers may be fulfilled.

The term "gross sales" shall not include any value received by lessee from the sale of used grease and used potato sacks, both of which are mere by-products of the operation of lessee's business.

The term "gross sales" as used herein shall also include the total gross income received by lessee from signs, displays, advertising, or any other activity conducted on or about the demised premises.

Exhibit No. 1-A—(Continued)

Notwithstanding the foregoing provisions, in the computation of "gross sales" there shall be excluded the amount of any sales tax paid by lessee to the State of California, the City of Los Angeles, County of Los Angeles, or the United States Government in respect to transactions which are included in the term "gross sales", whether or not the amount of such tax is collected as a separate item by the lessee from his customers.

V.

ABATEMENT OF RENTALS

Anything in this lease to the contrary notwithstanding, the guaranteed minimum monthly rental due and payable pursuant to the provisions of this lease shall abate during [309] the period of the planning and construction of said building; provided, however, that said period of abatement shall not exceed five months from the date of the execution of this lease; and during the said period of abatement the following rentals shall be due and payable in lieu of said guaranteed minimum monthly rentals:

(1) For the first and second months of the term of this lease no rent shall be due and payable;

(2) For the next three months of the term of this lease the sum of Five Hundred Dollars (\$500.00) per month shall be due and payable;

at the time provided for the payment of the guar-

Exhibit No. 1-A—(Continued)

anteed minimum monthly rental which is abated pursuant to the provisions of this paragraph.

* * * *

VII.

USE OF PREMISES

(a) The herein-demised premises shall be used by lessee solely and exclusively under the name "Carpenter's", for the purpose of carrying on a drive-in restaurant, cafe, and, at the option of lessee, a cocktail lounge, and for the sale and consumption of food, drinks, and all other articles of merchandise usually vended or sold from such establishments, and which are customarily sold in establishments of this character by the operators thereof in the City of Los Angeles, County of Los Angeles, State of California.

(b) The lessee expressly covenants and agrees that he will at all times maintain and conduct his business in a lawful manner, and in strict compliance and observance of all governmental rules, regulations, ordinances, or laws, and in strict compliance with all of the restrictions required to be observed by lessors upon the herein-demised property. In any [310] isolated instance of a failure of the lessee to comply with, fulfill, and observe any governmental rule, regulation, ordinance, or law, and such failure be brought to the attention of lessee, and lessee immediately remedy and rectify his failure in such respect, such original failure shall not constitute a breach on the part of lessee

Exhibit No. 1-A—(Continued)

of his covenants and agreements under this lease.

(c) Lessee hereby agrees, during the term of this lease, to operate and keep said business and said business establishment open during the usual business hours of each business day as may be customary in drive-in restaurants in the City of Los Angeles operating a business comparable to that permitted to be conducted by lessee hereunder. Lessee further agrees to conduct and carry on his business on the demised premises in accordance with the present method of conducting the drive-in restaurant establishments operated in the City of Los Angeles, State of California, under the name of "Carpenter's".

* * * *

IX.

UPKEEP AND REPAIRS

The lessee hereby covenants and agrees, at his own expense, to keep the said demised premises, th building, improvements, equipment, grounds, landscaping, and all parts thereof, and all lighting, glass, and fixtures in and upon the same, from and after the erection of the improvement herein contemplated, in good order, repair, and condition, externally and internally, as the same then are at the beginning of this lease, reasonable wear and tear and damages by fire, earthquake, tornado, or other unavoidable casualty only excepted; and it is expressly understood and agreed that lessors shall not be [311] under any obligation or expense

Exhibit No. 1-A—(Continued)

to make any repairs upon the demised premises, or any of the improvements thereon, or to replace or repair or to maintain any of the furniture, furnishings, equipment, or fixtures, but lessee alone shall be responsible therefor. If lessee fails to comply with this provision, lessors at their option may make such repairs and lessee shall repay lessors for such expenditures upon demand.

X.

FIRE INSURANCE

Lessee hereby covenants and agrees to keep insured against loss or damage by fire during the term of this lease any and all buildings or improvements that may be built upon or placed upon said premises, in a good and responsible company or companies doing business in the State of California, to an amount not less than eighty per cent (80%) of the value of said building or buildings, provided insurance in responsible companies doing business in the State of California can be obtained in that percentage, and, if not, then to the highest percentage that can be obtained less than the eighty per cent (80%).

Proceeds from any policy or policies shall be payable to both the lessors and the lessee as their interests may appear, and shall be used by them in trust for the uses and purposes herein after mentioned.

The original policies may be retained by the lessee, but the lessors shall have the right to inspect

Exhibit No. 1-A—(Continued)

any and all policies of fire insurance in the possession of the lessee in which the demised premises or the lessors are included, and the lessee, on demand, will furnish the lessors proof of payment of the premium on any such policies.

If at any time or times the lessee shall fail or [312] neglect to insure any of the premises or to cause the same to be insured as required by the provisions of this lease, then the lessors shall obtain such insurance in lessors' name or as the agent of the lessee in insurance companies satisfactory to said lessors. The amount of any premiums paid for such insurance obtained by the lessors as herein provided shall be forthwith due and payable from the lessee, with interest thereon at the rate of 6% per annum computed from the date of such payment.

XI.

DESTRUCTION OF BUILDING

The lessee hereby agrees that, in the event the premises shall be damaged or destroyed in whole or in part by fire, the elements, acts of God, other casualty or happening, and as often as the same shall occur, this lease and the term hereof shall be unaffected, except as to the abatement of rent hereinafter provided for, and shall continue in full force and effect, except that, if the premises shall be substantially destroyed during the last three years of the term of this lease, lessee shall have the option and privilege of cancelling and termi-

Exhibit No. 1-A—(Continued)

nating this lease upon giving notice to the lessors of such election within thirty days after the happening of any of the events aforesaid; and upon the giving of such notice this lease and the term hereof shall cease, terminate, and come to an end on the date specified in such notice therefor, which date shall be not sooner than twenty days after such notice is given; and both parties shall be and they are hereby released from and relieved of any and all liability and obligation hereunder which shall accrue after such date of termination.

The lessee hereby agrees, upon the happening of any of the events aforesaid, subject, however, to the lessee's [313] right of cancellation during the last three years of the term, to put the demised premises in as good order and condition as the same were in immediately preceding the happening of any of the events aforesaid, or to rebuild the same or construct a new building, as the case may reasonably require, with due diligence, delays occasioned by strikes, lock-outs, and other matters beyond the lessee's control or that of his contractors and materialmen, and delays reasonably occasioned in the settlement and adjustment of losses with insurance companies excepted.

If insurance moneys will be available for such losses as may have occurred, lessee shall have the right to adjust all of such losses without the consent or approval of the lessors, if the lessee so desires, and lessors will execute and deliver receipts or releases therefor as may be required by

Exhibit No. 1-A—(Continued)

the insurance companies; except that lessee will notify the lessors as to the amount of the adjustment on request; and the proceeds from the policies shall be paid to the lessee if the lessee does not elect to terminate this lease as hereinabove provided. If the lessee should terminate this lease as hereinabove provided, the lessors shall have the right to adjust all of such losses with the insurance companies without the consent or approval of the lessee, and shall be entitled to retain all of the proceeds of said insurance.

In the event business cannot be carried on on said demised premises by reason of the happening of any of the foregoing events, then the rentals due under the terms and provisions of this lease shall abate until the premises are in condition for the resumption of business thereon; provided, however, that such period of abatement shall not in any event exceed a period of four months. [314]

* * * *

XIII.

COVENANTS AGAINST LIENS

Lessee expressly covenants and agrees that he will not, during the term hereof, suffer or permit any lien to be attached to or upon said premises, or any portion thereof, by reason of any act or omission on the part of lessee, and hereby expressly agrees to save and hold harmless the lessors and their property from or against any such lien or claim of lien.

Exhibit No. 1-A—(Continued)

In the event any such lien does attach or any claim of lien is made against said demised premises which may be occasioned by any act or omission upon the part of lessee, and shall not be released within five (5) days, lessors, in their sole discretion, may pay and discharge the same and relieve the said demised premises from any such lien, and lessee agrees to repay and reimburse lessors for or on account of any expenses which may be incurred by lessors in discharging such lien or claims, or lessors may treat said default on the part of lessee as a breach of this lease, for which lessors shall be entitled to exercise and have any and all rights given to them in case of default under this lease or under any provision of law relating thereto.

* * * *

XIX.

TERMINATION ON ACCOUNT OF
INSOLVENCY OR RECEIVERSHIP

If any adjudication of bankruptcy or insolvency be made or rendered against lessee, or if a receiver of the business or assets of lessee should be appointed, or in the event of any attachment or execution being levied on the business or assets of lessee, and such attachment and/or execution is not removed within fifteen (15) days, or in the event of any sale or [315] attempted sale of the leasehold interest hereby created, under or by virtue of any execution or other legal or judicial order

Exhibit No. 1-A—(Continued)

or authority, the lessors may, at their option, with or without terminating this lease, enter and remove the lessee and all of the lessee's property from said demised premises, and no person, firm, or corporation shall have any right to use, possess, or occupy said demised premises or any part thereof under or by virtue of any matters or things herein in this paragraph set forth, without the written consent of lessors first had and obtained; provided, however, that neither the happening of any of the contingencies mentioned in this article nor the entry or re-entry of lessors nor the removal by lessors of lessee's property (in the happening of any such contingencies) shall constitute an election upon the part of lessors to terminate this lease, unless written notice to that effect is given by lessors to lessee, but in any event the happening of any such event shall constitute a default under this lease for which lessors shall have the same rights and remedies as provided in the case of any other default hereunder, or by any law relating thereto.

XX.

DEFAULT

In the event of default at any time by lessee in the payment of the rent herein provided for, for more than twenty (20) days, or in the performance of any other of his agreements herein contained, or if lessee vacate or abandon the demised premises for a period of ten (10) days, then in any or either of such events it shall be lawful for lessors,

Exhibit No. 1-A—(Continued)

after three (3) days' notice in writing to lessee of such default, to declare said demised term ended and to re-enter the premises or any part thereof either with or without process of law, lessee hereby waiving notice of any kind or any demand for possession of the demised premises, or [316] for the payment of rent; or lessors at their option, and without declaring the lease ended, may re-enter the premises and occupy or lease the whole or any part thereof for and on account of lessee and on such terms and conditions and for such rent as lessors may with reasonable diligence be able to secure, and may collect said rent or any other rent that may thereafter become payable and apply the same toward the amount due or thereafter to become due from lessee and on account of the expenses of such sub-letting and any and all other damages sustained by lessors. Should such rental be less than that herein agreed to be paid by lessee, lessee agrees to pay such deficiency to lessors, in advance, on the first day of each month hereinbefore specified for payment of rental, and to pay to lessors, forthwith upon any such re-letting, the costs and expenses lessors may incur by reason thereof.

Lessors may execute any such lease, either in their own names or in the name of lessee, as lessors may see fit, and the sub-tenant therein named shall be under no obligation whatsoever to see to the application by the lessors of any rent collected by lessors from such sub-tenant, nor shall lessee have

Exhibit No. 1-A—(Continued)

any right or authority whatever to collect any rent whatever from such sub-tenant.

Lessors shall not be deemed to have terminated this lease or the liability of lessee to pay the rent thereafter to accrue, or his liability for damages, by any such re-entry or by any action in unlawful detainer or otherwise, unless lessors notify lessee in writing that they have elected to terminate this lease; and lessee further covenants that the service by lessors of any notice pursuant to the unlawful detainer statutes of the State of California and the surrender of possession by lessee pursuant to such notice shall not (unless lessors elect to the contrary at the time [317] of or at any time subsequent to the service of such notice) be deemed to be a termination of this lease.

Nothing herein contained shall be construed as obligating lessors to sub-lease the whole or any part of the demised premises.

In the event of any entry and taking possession of the demised premises as aforesaid, lessors shall have the right but not the obligation to remove therefrom all or any personal property located therein and may place the same in storage at a public warehouse at the expense and risk of the owner or owners thereof.

It is further agreed by the parties hereto that after the service of notice or the commencement of a suit or after final judgment for the possession of said premises the lessors may receive and collect any rent due, and the payment of said rent shall not waive said notice, said suit, or said judgment.

Exhibit No. 1-A—(Continued)

XXIII.

ASSIGNMENT AND SUB-LETTING

Except as hereinafter provided, lessee shall not assign this lease or sub-let the whole or any part of the demised premises, or permit any other person, either jointly with the lessee or otherwise, to occupy the premises or any part thereof, without first obtaining on each occasion the written consent of lessor; and said lessee shall not sub-let the whole or any part of said demised premises, or permit any other person, either jointly with said lessee or otherwise, to occupy said premises or any part thereof without such written consent; and neither acceptance of rent by lessors from lessee or from any other person thereafter, nor the failure on the part of lessors for any particular period to take action on account of such breach or to enforce their rights, shall be deemed a waiver of the breach, but the same shall be a continuing breach as long as such sub-tenancy, assignment, or occupancy continues [318]

Lessors understand that it is the purpose of lessee to transfer the leasehold estate created by this lease to a corporation hereafter to be formed by lessee and other parties, and lessors hereby consent to the assignment of this lease to such corporation, provided that such corporation shall in writing assume and agree to perform each, every, and all of the terms, conditions, and covenants contained in this lease and to be performed by lessee herein,

Exhibit No. 1-A—(Continued)

and shall have sufficient assets or credit to enable it to erect the building as provided for herein. Upon the delivery of such written agreement of assumption by the new corporation, the lessee herein shall be released from all liability in connection with this lease, except any liability that shall devolve upon said lessee in his capacity as a stockholder or director of such corporation, or shall have accrued prior to such transfer.

* * * *

XXV.

LESSEE'S RIGHT TO TERMINATE

(a) If it becomes unlawful to maintain or operate a restaurant upon the demised premises, lessee may terminate this lease by written notice given to lessors promptly upon the establishment of that fact.

(b) If at any time the flow of vehicular traffic past the demised premises shall be substantially and permanently diminished as the direct result of the construction in the vicinity of the demised premises of any free-way or divided highway, or the permanent re-location, improvement, closing, or abandonment of Wilshire Boulevard or Western Avenue where the same front the demised premises, or the construction of any underpass, overpass, by-pass, tunnel, or subway at these points, except a pedestrian underpass or tunnel or tunnels, such as present school tunnels, [319] then lessee shall have the right to terminate this lease by thirty

Exhibit No. 1-A—(Continued)

days' written notice given to lessors promptly upon the establishment of that fact.

The foregoing option shall be available to lessee only if not in default hereunder.

Upon the termination of this lease as provided in this Paragraph (b), the ownership of the building constructed on said premises shall vest in the lessee, who shall be entitled to remove the same from the demised premises. If the same is not removed within thirty days after the termination of this lease, then and in that event title to said building shall revert to lessors herein.

XXVI.

LESSORS' RIGHT TO TERMINATE

Lessors shall have the right at any time during the last five years of the term of this lease of terminating the same upon thirty days' written notice to lessee of their election to terminate the lease and upon payment by lessors to lessee of the sum of Twenty-five Thousand Dollars (\$25,000.00) in cash, which said sum shall be payable at the time said notice of termination is served upon lessee.

XXVII.

OWNERSHIP OF BUILDING UPON
TERMINATION OF LEASE

Upon termination of this lease by reason of the expiration of the term hereof or by reason of the exercise of lessors' right to terminate as herein provided in Paragraph XXVI, or by any other

Exhibit No. 1-A—(Continued)

reason, title to the building erected on said property shall revert and belong to lessee, provided the lessee, at the time of such termination, is not in default in the [320] performance of any of the conditions, covenants, and provisions of this lease.

* * * *

XXXI.

HEIRS AND ASSIGNS

The covenants and conditions herein contained shall, subject to the provisions as to assignment, apply to and bind the heirs, successors, executors, administrators, and assigns of all the parties hereto; and all the parties hereto shall be jointly and severally liable hereunder.

* * * *

In Witness Whereof, the parties hereto have hereunto set their hands and seals, all as of the day and year first above written.

/s/ ROBERT ASHLEY PETTEY,

/s/ JULIA FAY PETTEY,

Trustees of the Estate of Mary Emma Pettey,
Deceased,

Lessors.

/s/ WILLIAM H. SIMON,

Lessee. [321]

Exhibit No. 1-A—(Continued)

State of California,
County of Los Angeles—ss.

On this 30th day of April, 1941, before me, Edith W. Olmstead, a Notary Public in and for said County and State, personally appeared Robert Ashley Pettey and Julia Fay Pettey, known to me to be the persons whose names are subscribed to the within instrument as Trustees of the Estate of Mary Emma Pettey, Deceased, and acknowledged to me that they executed the same as such Trustees.

(Seal) EDITH W. OLMSTEAD,
Notary Public in and for the County of Los Angeles, State of California.

My Commission Expires July 22, 1942.

State of California,
County of Los Angeles—ss.

On this 26th day of April, 1941, before me, Dorothy Block, a Notary Public in and for said County and State, personally appeared William H. Simon, known to me to be the person whose name is subscribed to the within instrument, and acknowledged to me that he executed the same.

(Seal) DOROTHY BLOCK,
Notary Public in and for the County of Los Angeles, State of California.

My Commission Expires December 9, 1941. [322]

EXHIBIT No. 2-B

SUPPLEMENT TO LEASE

This agreement, made and entered into this 2nd day of May, 1941, by and between Robert Ashley Pettey and Julia Fay Pettey, Trustees of the Estate of Mary Emma Pettey, Deceased, hereinafter called lessors; and William H. Simon, hereinafter called lessee;

Witnesseth:

Whereas, the parties hereto have heretofore executed that certain lease wherein and whereby lessors have leased to lessee for a period of fifteen years the following-described property, situated in the City of Los Angeles, County of Los Angeles, State of California:

Lots 1 and 2 in Block H of Westminster Place, as per map thereof recorded in the office of the County Recorder of the County of Los Angeles, State of California, in Book 9, Page 61 of Maps;

and

Whereas, said lease has not been delivered and, therefore, is not in full force and effect; and

Whereas, it is proposed to deliver said lease upon the execution of this supplemental agreement, which said supplemental agreement shall become a part of and be construed with that certain lease;

Now, therefore, in consideration of the payment of rents and performance of the covenants and

Exhibit No. 2-B—(Continued)

agreements contained in the above-mentioned lease and in this supplemental agreement, it is mutually agreed by and between the parties as follows:

(1) It is understood and agreed that the dimensions of the above-described demised premises are approximately 150 feet x 150 feet.

(2) Lessors agree, within sixty days after the [323] delivery of this lease, to remove all buildings and improvements from the demised premises and clear the same so that lessee may commence construction thereon.

When said premises have been cleared and are ready for construction lessors shall notify lessee in writing; and possession of said premises shall be deemed to have been delivered by lessors to lessee at the time said premises have been so cleared and said written notice delivered to lessee.

(3) Article V, on Page 5 of said lease, is hereby amended to read as follows:

“Anything in this lease to the contrary notwithstanding, the guaranteed minimum monthly rental due and payable pursuant to the provisions of this lease shall abate during the period the present improvements are being removed from said premises and during the period of the planning and construction of said building; provided, however, that said period of abatement shall not exceed five months from the date possession of said premises has been delivered to lessee as herein provided; and dur-

Exhibit No. 2-B—(Continued)

ing said period of abatement the following rentals shall be due and payable in lieu of said guaranteed minimum monthly rentals:

“(1) No rent shall be due and payable during the period the lessors are removing the present buildings from the premises and for a period of two months after possession of the premises has been delivered to lessee.

“(2) For the third, fourth, and fifth months after possession has been delivered to lessee, the sum of Five Hundred Dollars (\$500.00) per month shall be due and payable. Receipt of the rental for these three months is hereby acknowledged.”

(4) Article XV, of Page 14 of said lease, is hereby amended so that the first two lines of said article shall read as follows:

“Commencing with the day on which lessee starts to carry on business on the demised premises, or five months after the day possession of the premises is delivered to lessee, whichever date is the sooner”

(5) Article XXIII, on Page 20 of said lease, is hereby amended by the addition of the following paragraph: [324]

“After the above-mentioned corporation has been formed and the restaurant building constructed and erected on the demised premises, and this lease assigned to said corporation, lessors hereby agree and consent to said cor-

Exhibit No. 2-B—(Continued)

poration's sub-letting to a partnership which will operate the restaurant on the demised premises; provided, however, that said partnership shall operate said restaurant under the name of "Carpenter's" and conducts and carries on the business on the demised premises in accordance with the present method of conducting the drive-in restaurant establishments operated in the City of Los Angeles, State of California, by Harry B. Carpenter."

In Witness Whereof, the parties hereto have hereunto set their hands and seals, all as of the day and year first above written.

/s/ ROBERT ASHLEY PETTEY,

/s/ JULIA FAY PETTEY,

Trustees of the Estate of Mary
Emma Pettey, Deceased,
Lessors.

/s/ WILLIAM H. SIMON,

Lessee. [325]

EXHIBIT No. 3-C

CONSENT TO MEETING AND WAIVER OF
NOTICE THEREOF

We, the undersigned, being the persons named as directors in the Articles of Incorporation of Wilshire and Western Sandwiches, Inc., a corporation organized under the laws of the State of California, do hereby consent to the holding of the first

Exhibit No. 3-C—(Continued)

meeting of the incorporators at Room 307, 649 So. Olive Street, in the City of Los Angeles, State of California, on July 14, 1941, at the hour of 4:00 p.m., for the purpose of adopting by-laws, electing officers, and for the transaction of any other business pertaining to said corporation and its affairs which may come before said meeting; and the undersigned and each of them hereby waive written notice of the time and place of the holding of said meeting.

Los Angeles, California, July 14, 1941.

HARRY B. CARPENTER,
M. A. McDONNELL,
WM. H. SIMON,
MIKE LYMAN,
G. C. JOBSON.

[326]

MINUTES OF FIRST MEETING OF
BOARD OF DIRECTORS

Of Wilshire and Western Sandwiches, Inc., a
California Corporation

The directors named in the Articles of Incorporation of Wilshire and Western Sandwiches, Inc., a California corporation, held their first meeting at Room 307, No. 649 So. Olive Street, in the City of Los Angeles, California, on the 14th day of July, 1941, at the hour of 4:00 o'clock p.m. of said day.

Present at said meeting: Harry B. Carpenter, M. A. McDonnell, William H. Simon, Mike Lyman,

Exhibit No. 3-C—(Continued)

and G. C. Jobson, being all of the directors of said corporation named in its Articles of Incorporation.

On motion and by unanimous vote, Mr. Harry B. Carpenter was elected temporary Chairman and Mr. G. C. Jobson was elected temporary Secretary of the meeting.

The Chairman announced that the meeting was held pursuant to written Waiver of Notice thereof and Consent thereto, signed by all of the directors of the corporation named as such in the Articles of Incorporation. Such waiver and consent was presented to the meeting and upon motion made and unanimously carried, was made a part of [327] the records of the meeting, and now precedes the minutes of this meeting in the book of minutes of the corporation.

The Chairman stated that the original Articles of Incorporation had been filed in the Office of the Secretary of State of the State of California, on the 24th day of March, 1941, and that a copy thereof, certified by the Secretary of State, had been filed in the office of the County Clerk of Los Angeles County, California, on the 31st day of March, 1941, being the county in which the corporation is to have its principal office. He presented to the meeting a copy of said Articles of Incorporation, showing filings as stated, and the secretary was directed to insert said copy in the book of minutes of said corporation.

The matter of the adoption of by-laws for the

Exhibit No. 3-C—(Continued)

regulation of the affairs of the corporation was next considered. The Secretary presented to the meeting a form of by-laws, which were duly considered and discussed. On motion duly made and unanimously carried, the following resolutions were adopted, to wit:

Resolved; That the by-laws presented to this meeting and discussed thereat be, and the same hereby are adopted as and for the by-laws of this corporation.

Resolved Further; That the Secretary of this corporation be, and he hereby is authorized and directed to execute a certificate of the adoption of said by-laws and to insert said by-laws as so certified in the book of minutes of this corporation, and to see that a copy of said by-laws, similarly certified, is kept at the principal office for the transaction [328] of business of this corporation, in accordance with Section 302 of the Civil Code of the State of California.

The meeting then proceeded to the election of officers. The following were duly elected to the offices indicated after the names of each:

1. President: Mr. Harry B. Carpenter.
2. Vice-President: Mr. William H. Simon.
3. Secretary-Treasurer: Mr. Harry B. Carpenter, Jr.

Each officer so elected, being present, accepted his office, and thereafter the President presided at

Exhibit No. 3-C—(Continued)

the meeting as Chairman and the Secretary acted as Secretary of the meeting.

The Secretary presented for the approval of the meeting a proposed seal of the corporation, consisting of two concentric circles with the words, "Wilshire and Western Sandwiches, Inc., California", and the words and figures, "Incorporated March 24, 1941", in the form and figure as follows:

On motion duly made and unanimously carried, the following resolution was adopted:

Resolved; That the corporate seal, in the form, words and figures presented to this meeting, be and the same hereby is adopted as the seal of this corporation.

The Secretary presented to the meeting a proposed form of share certificate for use by the corporation. On motion [329] duly made and unanimously carried, said form of share certificate was approved and adopted, and the Secretary was instructed to insert a copy thereof in the book of minutes immediately following the minutes of the meeting.

Mr. William H. Simon, one of the original incorporators, was present at the meeting. He stated that he had acquired a lease, dated April 26, 1941, and a supplement thereto, dated May 2, 1941, from Robert Ashley Pettey and Julia Fay Pettey, trustees of the Estate of Mary Emma Pettey, deceased, hereinafter referred to as "lease", leasing to him certain real property situate at the north-

Exhibit No. 3-C—(Continued)

west corner of Wilshire Boulevard and Western Avenue, in the City of Los Angeles, County of Los Angeles, State of California, more particularly described as:

Lots 1 and 2 in Block H of Westminster Place, as per map thereof recorded in the office of the County Recorder of the County of Los Angeles, State of California, in Book 9, Page 61 of Maps.

said lease being for a period of fifteen years beginning April 30, 1941, and ending April 29, 1956, and providing for a percentage rental of six per cent of the total gross sales made in connection with the business conducted in on or from the demised premises with the provision that said rental shall not be less than \$700 each month during the term of said lease, and containing other provisions, as more fully appears by said lease; and that said lease further provides that the same may be assigned to a corporation formed in which he would be one of the incorporators, in such [330] event the corporation to accept such assignment and agree in writing to be bound by and carry out and perform all the covenants of the lease to the same extent as if the said corporation had been originally named in the lease in the place and stead of said Simon, and in such event said Simon to be released from all personal liability under the lease. Said Simon thereupon exhibited and presented said lease to the meeting. Said Simon proposed to assign said lease to this corporation, and all his

Exhibit No. 3-C—(Continued)

right, title and interest therein, upon this corporation assuming said lease and paying to him the amount of any costs and expenses which he may have incurred in acquiring said lease, and assuming his obligation for the construction of said building upon said premises. He further stated that it had been agreed among the incorporators that, in the event of the assignment of the said lease to this corporation, it would proceed with the erection of a drive-in sandwich stand and the equipment thereof and that the incorporators would purchase stock to the extent of at least \$15,000 and, thereafter, individually lend to the corporation a sufficient sum to enable it to complete the erection and construction of said drive-in sandwich stand on said premises and the equipment thereof.

Thereupon, the following resolution was unanimously adopted: [331]

“Whereas William H. Simon has offered to assign and transfer to this corporation that certain lease dated April 25, 1941, between Robert Ashley Pettey and Julia Fay Pettey, trustees of the Estate of Mary Emma Pettey, deceased, as Lessors, and William H. Simon, as Lessee, whereby the Lessors leased to the Lessee the certain premises at the northwest corner of Wilshire and Western Avenue in the City of Los Angeles, to wit:

Lots 1 and 2 in Block H of Westminster Place, as per map thereof recorded in the

Exhibit No. 3-C—(Continued)

office of the County Recorder of the County of Los Angeles, State of California, in Book 9, Page 61 of Maps.

(which said lease has been exhibited to and considered by the Board of Directors of this corporation at this meeting) upon the condition that this corporation accept the assignment of said lease and agree to be bound by and perform all of the terms and conditions thereof;

Now, Therefore, Be It Resolved that this corporation accepts said proposal and authorizes the President and the Secretary of this Corporation to execute its written acceptance of the assignment of said lease and its written agreement to be bound by and to perform all of the covenants and conditions of said lease.

Carried, all of the Directors voting "Aye".

On motion duly made and seconded and unaniously carried it was resolved that the President and Secretary of this corporation be and they are hereby authorized to make application in the name of this corporation to the Commissioner of Corporations of the State of California for a permit to issue and sell at this time to the original incorporators \$15,000 of the capital stock of this corporation, at par, for cash, and also for a permit authorizing this corporation to sell to the original incorporators all the balance of its capital stock, at

Exhibit No. 3-C—(Continued)

par, for cash, at such times as may be from time to time ordered [332] by the Board of Directors.

The President stated that it was necessary for this corporation to fix and establish a taxable year for federal and state income tax purposes. Whereupon, on motion duly made, seconded, and unanimously carried, the following resolution was adopted:

Resolved; That this corporation shall, and the Board of Directors thereof does, hereby fix the taxable year of this corporation for Federal and State income tax purposes as being from January 1st to and including December 31st of each and every calendar year, and that the first of said taxable years shall be the year 1941 and such taxable year shall end on December 31, 1941.

To provide for a depository for the funds of the corporation and to authorize certain officers to deal with the corporation funds, the following resolution was duly adopted:

Resolved; That the funds of this corporation be deposited with the Bank of America National Trust & Savings Association, Wilshire and Western Branch, 635 South Western Avenue, Los Angeles, California.

Resolved Further; That all checks and drafts shall be signed by the President, Harry B. Carpenter, or the Secretary, Harry B. Car-

Exhibit No. 3-C—(Continued)

penter, Jr., and all other instruments obligating this corporation to pay money shall be signed on behalf of this corporation by the President and Secretary, or by any two of the President, Vice-President and Secretary.

There being no further business to come before the board, on motion duly made, seconded and unanimously carried, the meeting adjourned.

HARRY B. CARPENTER, JR.,
Secretary.

Approved:

HARRY B. CARPENTER,
President. [333]

EXHIBIT No. 4-D

Before the Division of Corporations, Department
of Investment of the State of California

No.

In the Matter of

WILSHIRE & WESTERN SANDWICHES,
Inc., a corporation

Application for Leave to
Issue Capital Stock

APPLICATION FOR PERMIT

To the Honorable Commissioner of Corporations
of the State of California:

The petitioner, Wilshire and Western Sand-

Exhibit No. 4-D—(Continued)

wiches, Inc., a corporation, respectfully represents as follows:

I.

That petitioner is a corporation organized and existing under and by virtue of the laws of the State of California, having its principal place of business in the City of Los Angeles, County of Los Angeles, State of California.

II.

That its Articles of Incorporation were duly filed in the office of the Secretary of State of the State of California [334] on March 24, 1941. That a copy of said Articles of Incorporation was duly filed in the office of the County Clerk in and for the County of Los Angeles, State of California, on March 31, 1941. That a copy of said Articles of Incorporation is hereto annexed, marked Exhibit "A" and made a part of this application.

III.

That the principal office of said corporation is in the County of Los Angeles, State of California, and its principal post office address is 3180 West Sixth Street, Los Angeles, California.

IV.

That the name of its attorneys in the matter of this proceeding is Tanner, Odell & Taft, 524 Van Nuys Building, Los Angeles, California.

V.

That the active business of said corporation will be carried on by the following persons, who are officers and directors of the corporation:

Exhibit No. 4-D—(Continued)

Harry B. Carpenter, President, 625 Cumberland Road, Glendale, California.

Wm. H. Simon, Vice-President, 9515 Heather Road, Los Angeles, California. [335]

Harry B. Carpenter, Jr., Secretary-Treasurer, 1945 West Mountain Street, Glendale, California.

VI.

That the corporation has duly adopted by-laws for the government of said corporation. That a copy of said by-laws is hereto annexed, marked Exhibit "B", and made a part of this application.

VII.

That a copy of all minutes relating to or affecting the issuance of securities by the corporation, namely, a portion of the minutes of a meeting of the corporation held on the 14th day of July, 1941, is hereto annexed, marked Exhibit "C" and made a part of this application.

VIII.

That the purpose for which the corporation has been organized is to carry on and operate a drive-in sandwich restaurant and for that purpose to lease real estate or to acquire a lease thereon, and to erect thereon the necessary buildings and structures with the accessories for the establishment, carrying on and maintenance of said business and to equip the same with all the necessary equipment and paraphernalia. It is proposed to sell and issue at this time 1500 shares of the [336] common stock of the corporation for the purpose of raising money to erect a building and such other structures

Exhibit No. 4-D—(Continued)

as may be necessary for the conduct of said business and to pay the expenses of incorporation and of making this application not to exceed \$500, and to borrow from the individual stockholders or incorporators additional money sufficient to complete such buildings and equip the same and furnish it as may be needed in the conduct of the business. It is proposed also to sell additional of its stock for cash and to the incorporators if it should become necessary to do so for the purpose of completing the building or equipment or for further expanding the business or facilities thereof.

IX.

That a copy of the certificate of stock proposed to be issued by said corporation is hereto annexed, marked Exhibit "D" and made a part of this application.

X.

That it is proposed to sell 1500 shares of said stock to the particular persons hereinafter named and not to the public. That the sales of stock are to be made for cash, lawful money of the United States, to be paid into the treasury of the corporation. That no commission will be paid for the [337] sale of any of said stock and no prospectus or advertising of any kind will be used. That it is proposed to sell said stock immediately upon the issuance of a permit to issue the same.

XI.

That the names and addresses of the officers of the corporation are as follows:

Exhibit No. 4-D—(Continued)

Harry B. Carpenter, 625 Cumberland Road, Glendale, California.

Wm. H. Simon, 9515 Heather Street, Los Angeles, California.

Harry B. Carpenter, Jr., 1945 West Mountain Street, Glendale, California.

The qualifications of the officers who will have charge of the business are as follows:

Harry B. Carpenter has been engaged in the restaurant business for over thirty years and has operated as a restaurateur and in the conduct of restaurant business, both individually and in association with others during the whole of said period.

Wm. H. Simon has been engaged in the restaurant business individually and in association with others for over twenty-five years.

Harry B. Carpenter, Jr., twenty-seven years of age, has been employed by his father, Harry B. Carpenter, for approximately eight years in connection with the operation of drive-in sandwich restaurants, and has served as manager of one of [338] such establishments for said Harry B. Carpenter, Sr., for about six years and has been president of Carpenter's Sandwiches, Inc., since on or about September 1, 1937, and in active charge of the operations of the sandwich stand and restaurant conducted by said Carpenter's Sandwiches, Inc. For several years he has also had charge of accounts and bookkeeping in connection with the drive-in sandwich restaurants operated by Harry B. Carpenter.

Exhibit No. 4-D—(Continued)

XII.

No itemized account of the financial condition of said corporation is hereto attached for the reason that it has as yet no assets and no liabilities and has not done any business.

XIII.

The date upon which the corporation proposes to commence to sell its securities is within five days after the granting of this application.

XIV.

The number, kind and amount of the securities said corporation proposes to sell is as follows:

1500 shares for cash. [339]

5000 shares in such amounts and at such times thereafter as may be authorized by the Board of Directors of said corporation, the same to be sold to the said original incorporators for cash. The par value of said stock is \$10 per share and the price at which it proposes to sell its securities is the same.

Wherefore, Petitioner prays that a permit be issued authorizing the applicant to sell 1500 shares of its capital stock to: Harry B. Carpenter, M. A. McDonnell, Wm. H. Simon, Mike Lyman, G. C. Jobson, for \$15,000 cash, the same to be sold and issued to them in such proportions or amounts as they may determine, and further permitting said applicant to issue the remaining 6000 shares to said original incorporators for cash to be paid to them at the time of issuance at the full par value

Exhibit No. 4-D—(Continued)

of stock so issued, the same to be issued for cash as aforesaid from time to time as may be directed and ordered by the Board of Directors.

Very respectfully,

(Seal)

WILSHIRE AND WESTERN
SANDWICHES, INC.,

By HARRY B. CARPENTER,
President.

By HARRY B. CARPENTER, JR.
Secretary. [340]

State of California,
County of Los Angeles—ss.

Harry B. Carpenter, being duly sworn on oath deposes and says that he is the President and one of the directors of Wilshire and Western Sandwiches, Inc., a corporation, mentioned in the within application, and knows the contents thereof and that the statements therein are true.

HARRY B. CARPENTER.

Subscribed and sworn to before me this 14th day of July, 1941.

ROBERT A. ODELL,
Notary Public in and for the County of Los Angeles, State of California. [341]

EXHIBIT No. 5-E

Copy

Before The Department of Investment, Division of
Corporations of the State of California

In the matter of the application of

WILSHIRE & WESTERN SANDWICHES,
INC.,

for a permit authorizing it to sell and issue its
securities.

PERMIT

File No. 73136 LA

Receipt No. LA A7394

This permit does not constitute a recommendation or endorsement of the securities permitted to be issued, but is permissive only Wilshire and Western Sandwiches, Inc., a California corporation, is hereby authorized to sell and issue its securities as hereinbelow set forth:

1. To sell and issue to Harry B. Carpenter, M. A. McDonnell, Wm. H. Simon, Mike Lyman, and G. C. Jobson, or to any or all of them, an aggregate of not to exceed 7,500 shares, at par, for cash, lawful money of the United States, for the uses and purposes recited in its application, and so as to net applicant the full amount of the selling price thereof.

This permit is issued upon the following condition:

(a) That unless revoked, suspended, or renewed upon application filed on or before the date of expiration specified in this condition, all authority to sell and issue securities under issuance clause 1 of this permit shall terminate and expire on the 17th day of January, 1942.

Dated Los Angeles, California, July 17, 1941.

(Seal) EDWIN M. DAUGHERTY,
Commissioner of Corporations,

By /s/ RONALD H. LOENHOLM,
Deputy.

JFO'D:EM

Corp. Form A-2

[342]

EXHIBIT No. 6-F

ASSIGNMENT AND ASSUMPTION
OF LEASE

This Agreement made and entered into this 14th day of July, 1941, by and between Wm. H. Simon, hereinafter referred to as "Assignor", and Wilshire and Western Sandwiches, Inc., a California Corporation, hereinafter referred to as "Assignee,"

Witnesseth:

Whereas, on or about the 2nd day of May, 1941, Assignor and Robert Ashley Pettey and Julia Fay Pettey, Trustees of the estate of Mary Emma Pettey, deceased, entered into a certain written lease agreement dated April 26, 1941 and a certain written Supplemental Lease Agreement dated May 2,

1941, wherein and whereby the said Robert Ashley Pettey and Julia Fay Pettey, as Trustees of the estate of Mary Emma Pettey, leased to Assignor for a term of fifteen (15) years, commencing on the 30th day of April, 1941, the following described premises.

Lots 1 and 2 in Block H of Westminster Place, as per map thereof recorded in the office of the County Recorder of the County of Los Angeles, State of California, in Book 9, Page 61 of Maps.

Now, Therefore, in consideration of the mutual covenants herein contained and other good and valuable consideration, the parties hereto agree as follows:

1. Assignor does by these presents grant, bargain, sell, assign, transfer, and set over unto Assignee all of the right, title and interest of Assignor in and to the above-described lease.

2. Assignee does hereby expressly accept and assume and agree to perform each, every, and all of the conditions, [343] covenants, and obligations contained in said lease to be kept and performed by the lessee therein, and does expressly agree to perform and be bound by all of the agreements, restrictions, and conditions of said lease on the part of the lessee to be kept and performed, the same as if this corporation had been originally named in said lease in the place and stead of assignor.

In Witness Whereof, assignor has hereunto set

his hand and assignee has caused this agreement to be executed by its officers thereunto duly authorized, and its corporate seal to be hereunto affixed; all as of the day and year first above written.

/s/ WM. H. SIMON,
Assignor,

WILSHIRE AND WESTERN
SANDWICHES, INC.,
a California corporation,

By HARRY B. CARPENTER,
President.

(Seal) By HARRY B. CARPENTER, JR.,
Secretary Assignee.

We hereby consent to the foregoing assignment.

Dated August 14, 1941.

/s/ ROBERT ASHLEY PETTEY,

/s/ JULIA FAY PETTEY,
Trustees of the Estate of Mary Emma Pettey, deceased. [344]

State of California,
County of Los Angeles—ss.

On this 21st day of August, 1941, before me, Alvin M. Sidman, a Notary Public in and for said County, personally appeared Wm. H. Simon,

known to me to be the person whose name is subscribed to the within instrument and acknowledged to me that he executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year in this certificate first written.

(Seal) ALVIN M. SIDMAN,
Notary Public in and for said County and State.

My Commission expires July 17, 1945.

State of California,
County of Los Angeles—ss.

On this 28 day of August, 1941, before me, Robert A. Odell, a Notary Public in and for said County, personally appeared Harry B. Carpenter, known to me to be the President, and Harry B. Carpenter, Jr., known to me to be the Secretary of Wilshire and Western Sandwiches, Inc., the corporation that executed the within instrument known to me to be the persons who executed the same on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

Witness My Hand and Official Seal.

ROBERT A. ODELL,
Notary Public in and for said County and State.

EXHIBIT No. 7-G

Copy

LEASE

This Lease, made and entered into this 22nd day of August, 1931, by and between Edna R. Vogel as Lessor and Wilshire-Western Sandwiches, Inc., as Lessee:

Witnesseth:

That, in consideration of the payments of rents and the performance of other covenants and agreements herein provided to be performed by the Lessee, the Lessor has leased and demised unto the Lessee the premises situated in the City of and County of Los Angeles, State of California, particularly described as follows:

Lot 15 Block "H" Westminster Place, as per map thereof recorded in Book 9 Page 61 of Maps, in the office of the County Recorder of said County; said property being known as 640 South Manhattan Place;

together with all the rights, easements and appurtenances to the real property belonging and appertaining and usually had and enjoyed therewith; subject however, to the terms, conditions, exceptions, reservations and restrictions herein mentioned or contained.

The term of this lease shall be for fourteen (14) years and eight (8) months commencing on the first day of September, 1941 and ending on the 29th day of April, 1956.

Exhibit No. 7-G—(Continued)

Lessee hereby agrees to pay a rental for said premises during the entire period of this lease of Sixty (\$60) Dollars per month, payable monthly in advance on the first day of each and every calendar month of the term of this lease. In addition to said monthly rental of Sixty (\$60) Dollars, Lessee [346] hereby covenants and agrees to pay, prior to delinquency, all of the taxes, City, County or State, levied or assessed upon demised premises and upon any improvements placed thereon by Lessee and upon any personal property, furniture or equipment owned by Lessee or stored or used on the demised premises; and all lighting assessments thereon.

Compensation and Liability Insurance:

Lessee hereby agrees that it will maintain an insurance policy with a responsible company and at its own expense, insuring Lessor against all liability for damages which may be occasioned to any persons or property while on said demised premises and agrees to indemnify Lessor for any damage or liability which they may incur or from any demands or liability, causes of action or expense to which Lessor may be put by reason of any injury to persons or property resulting from the use or operation of the demised premises. Lessee also agrees to furnish Lessor a copy of said liability insurance policy.

Assignment and Sub-Letting:

Lessee may assign this lease or sub-let the whole or any part of said premises providing Lessee

Exhibit No. 7-G—(Continued)

continue to assume the same responsibility as to payment of rents and the conditions and provisions herein contained.

Covenants Against Liens:

Lessee covenants and agrees that it will not during the term hereof, permit any lien to be placed upon said premises and will hold harmless the Lessor and her property against any lien. [347]

Use of Premises:

The herein demised premises may be used by Lessee for any purpose not prohibited by governmental regulation, ordinances or laws.

Insolvency or Receivership:

If any adjudication of bankruptcy or insolvency be rendered against the Lessee or if a receiver of the business or assets of the Lessee shall be appointed, or it shall be attached, or if any sale or attempted sale of the leasehold interest hereby created shall be made under or by virtue of any execution or other judicial process, the Lessor shall have the right to immediately terminate this lease, and no person shall have the right to use, possess or occupy the said premises by virtue thereof.

Default:

In the event of default at any time by Lessee in the payment of the rent herein provided for, for more than twenty (20) days, or in the performance of any other of its agreements herein contained, or if Lessee vacate or abandon the demise premises for a period of ten (10) days, then in any or either of such events it shall be lawful for Lessor, after

Exhibit No. 7-G—(Continued)

three (3) days' notice in writing to Lessee of such default, to declare said demised term ended and to re-enter the premises or any part thereof either with or without process of law.

Possession of Premises:

Lessor hereby agrees to permit Lessee to remove the garage now on said premises in order that Lessee may begin work on its contemplated improvements on the Easterly fifty (50) feet of said premises, at any time after the execution of this lease; Lessor further agrees to remove all other [348] buildings from said premises not later than September 15, 1941.

Ownership of Building:

Upon the termination of this lease by reason of the expiration of the term hereof or by any other reason, title to the buildings erected on said property shall revert to and belong to Lessee, provided the Lessee, at the time of such termination is not in default in the performance of any of the conditions, covenants and provisions of this lease. it being understood however that if this lease is terminated for any reason at any time before April 29, 1956, said buildings are not to be removed by the Lessee without first obtaining the written consent of the Lessor. In the event of the removal of said buildings, Lessee hereby agrees to leave the lot in a level and satisfactory condition.

Exhibit No. 7-G—(Continued)

Utilities:

Lessee Further agrees to pay promptly and prior to delinquency all charges incurred by lessee in the conduct or operation of its said business on the demised premises for gas, water, electricity, telephone and all other expenses and charges it may have, and for any and all other public utilities furnished to or which may be used upon the whole or any part of the herein demised premises.

Place for Payments of Money and Notices:

All payments of rental due hereunder shall be paid to Lessor at 754 North New Hampshire Avenue, Los Angeles, California, or at such other place as Lessor may from time to time designate in writing.

Service of any notice or notices or demands required or permitted to be given hereunder shall be sufficient if delivered to Lessor personally or duly authorized representative of Lessee personally, or if sent by United States Registered [349] Mail, postage prepaid, to Lessor, addressed to 754 North New Hampshire Avenue, Los Angeles, California or elsewhere as Lessor may from time to time designate in writing, or to Lessee, addressed to the demised premises or to 3180 West 6th Street, Los Angeles, California, or elsewhere as Lessee may from time to time designate in writing.

Payment of Money:

All sums of money to be paid by Lessee hereunder shall be payable in coin or currency which

Exhibit No. 7-G—(Continued)

at the time of payment is legal tender in the United States of America for public or private debts.

Holding Over:

Any holding over after the expiration of the said term, with the consent of the Lessor, shall be construed to be a tenancy from month to month, at a minimum rental of One Hundred (\$100) Dollars a month, and shall otherwise be on the terms and conditions herein specified, so far as applicable.

Heirs and Assigns:

The covenants and conditions herein contained shall, subject to the provisions as to assignment, apply to and bind the heirs, successors, executors, administrators and assigns of all the parties hereto; and all the parties hereto shall be jointly and severally liable hereunder.

In Witness Whereof, the parties hereto have hereunto set their hands and seals, all as of the day and year first above written.

/s/ EDNA R. VOGEL,
Lessor.

WILSHIRE-WESTERN
SANDWICHES, INC.,
Lessee,

By /s/ HARRY B. CARPENTER,
President.

Corporate Seal.

Exhibit No. 7-G—(Continued)

State of California,
County of Los Angeles—ss.

On this 22nd day of August, 1941, before me, Edith W. Olmstead, a Notary Public in and for said County and State, personally appeared Edna R. Vogel, known to me to be the person whose name is subscribed to the within instrument and acknowledged to me that she executed the same.

In Witness Whereof, I have hereunto set my hand and seal the day and year in this certificate first above written.

(Seal) /s/ EDITH W. OLMSTEAD,
Notary Public in and for said County and State.

My Commission expires July 22, 1942.

State of California,
County of Los Angeles—ss.

On this 22nd day of August, 1941, before me, Edith W. Olmstead, a Notary Public in and for said County and State, personally appeared Harry B. Carpenter, known to me to be President of Wilshire-Western Sandwiches, Inc., the corporation that executed the within instrument, known to me to be the person who executed the within Instrument, on behalf of the Corporation herein named, and acknowledged to me that such Corporation executed the same.

In Witness Whereof I have hereunto set my

Exhibit No. 7-G—(Continued)

hand and affixed my official seal the day and year in this certificate first above written.

(Seal) /s/ EDITH W. OLMSTEAD,
Notary Public in and for said County and State.

My Commission expires July 22, 1942.

[Endorsed]: Filed Dec. 3, 1947. [351]

[Title of Tax Court and Cause.]

ORDER RE TRANSMISSION OF EXHIBITS
IN ORIGINAL FORM

For cause appearing of record, it is

Ordered that Joint Exhibits 8-H, 9-I and 10-J inclusive referred to in Item 6 of petitioner's designation of record be transmitted with the appeal record by the Clerk of The Tax Court of the United States to the Clerk of the U. S. Court of Appeals for the Ninth Circuit as physical documents.

/s/ BOLON B. TURNER,
Judge.

Dated Washington, D. C., October 7, 1948. [352]

[Title of Tax Court and Cause.]

ORDER RE TRANSMISSION OF EXHIBITS
IN ORIGINAL FORM

Upon consideration of the motion filed by the respondent in the above case for transmission of original exhibits to the United States Court of Appeals for the Ninth Circuit, it is

Ordered that petitioner's Exhibits 11 to 31, both inclusive, constituting part of the record on review in this proceeding, remain in the custody of the Clerk of The Tax Court of the United States until fifteen days before the cause is set for argument in the United States Court of Appeals for the Ninth Circuit, at which time, upon request of counsel for either party, the Clerk of The Tax Court shall transmit the original Exhibits 11 to 31, inclusive, to the Clerk of United States Court of Appeals for the Ninth Circuit, in physical form.

/s/ BOLON B. TURNER,
Judge.

Dated Washington, D. C., October 12, 1948. [353]

In the United States Circuit Court of Appeals
For the Ninth Circuit

Tax Court Docket No. 10638

WILSHIRE & WESTERN SANDWICHES,
INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

To the Clerk of The Tax Court:

You will please transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit copies duly certified as correct of the following documents and records in the above entitled cause in connection with the petition for review by said Circuit Court of Appeals for the Ninth Circuit heretofore filed by Wilshire & Western Sandwiches, Inc.:

1. Docket entries of the proceedings before the Tax Court.

2. Pleadings before the Tax Court:

(a) The petition including the annexed copy of the deficiency letter.

(b) The answer.

(c) The taxpayer's motion to amend the petition to conform to the proof.

(d) Amendment to the petition. [354]

(e) Answer to the amendment to the petition.

3. Findings of fact, opinion and decision of the Tax Court.

(a) Findings of fact and opinion promulgated June 29, 1948.

(b) Judgment entered on or about June 29, 1948.

4. Petition for review of the decision of the Tax Court and assignment of error, together with proof of service of notice of filing the petition for review and of service of a copy of the petition for review.

5. One copy of the transcript of the hearings had before the Tax Court at Los Angeles, California, on December 3, 4 and 12, 1947 and the deposition of Robert A. Odell, together with all stipulations of fact.

6. All exhibits filed in evidence including both those made a part of the stipulation of facts and those filed in evidence during the course of the hearing are to be transmitted to the Clerk of the Circuit Court of Appeals of the Ninth Circuit in physical form. [355]

7. This praecipe.

SWARTZ, TANNENBAUM,
ZIFFREN & STEINBERG
and JACOB SHEARER,

By /s/ JACOB SHEARER,
Attorneys for Petitioner.

Service of a copy of the within proceeding is hereby admitted this 6th day of October, 1948.

/s/ CHARLES OLIPHANT,
Chief Counsel,
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Oct. 6, 1948. [356]

The Tax Court of the United States
Washington

Docket No. 10638

WILSHIRE & WESTERN SANDWICHES,
INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CERTIFICATE

I, Victor S. Mersch, clerk of The Tax Court of the United States do hereby certify that the foregoing pages, 1 to 356, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 14th day of October, 1948.

/s/ VICTOR S. MERSCH,

Clerk, The Tax Court of the United States.

[Endorsed]: No. 12079. United States Court of Appeals for the Ninth Circuit. Wilshire & Western Sandwiches, Inc., Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed October 29, 1948.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for
the Ninth Circuit.

In the United States Court of Appeals
For the Ninth Circuit

Case No. 12079

WILSHIRE & WESTERN SANDWICHES,
INC., a corporation,

Petitioner on Review,
vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

STATEMENT OF POINTS UPON WHICH
PETITIONER INTENDS TO RELY

Comes now the Petitioner, Wilshire & Western Sandwiches, Inc., a corporation, and cites the following points upon which it intends to rely for reversal of the judgment of the Tax Court, Hon. Richard L. Disney, Judge:

1. The Tax Court erred in holding that the sum of Fifteen Hundred Dollars (\$1500) accrued in

the year 1942 and of One Thousand Four Hundred Forty-Three and 26/100 Dollars (\$1,443.26) accrued in the year 1943 and paid by the taxpayer as interest on loans by its shareholders, was not deductible as interest on an indebtedness.

2. The Tax Court erred in refusing to hold that said sums set forth above were interest on an indebtedness and as such were deductible from the taxpayer's gross income in determining its net income subject to taxation.

3. The Tax Court erred in determining that there was a deficiency in the taxpayer's income taxes for the taxable years 1942 and 1943.

4. The Tax Court erred in determining that there was a deficiency in the taxpayer's excess profits taxes for the taxable year 1943.

5. The Tax Court erred in determining that there was a deficiency in the taxpayer's declared value excess profits taxes for the year 1943.

The Petitioner designates the entire record as certified by the Tax Court to the Circuit Court of Appeals for the Ninth Circuit as necessary for a consideration of the points upon which it intends to rely.

Dated this day of November, 1948.

SWARTS, TANNENBAUM,
ZIFFREN & STEINBERG,
and JACOB SHEARER.

By /s/ DAVID TANNENBAUM,
Attorney for Petitioner.

[Endorsed]: Filed November 4, 1948. Paul P. O'Brien, Clerk.

